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reprints of current materials on
economic and social development

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Frances M. Geiger, DIGEST Editor

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AGRARIAN REFORM

Agrarian reform is an important aspect of modernization in a number of developing countries. However, initial expectations regarding the ease and speed with which it could be accomplished have proven unrealistic in all but a very few countries. Most are making progress much more slowly and are finding obstacles and problems much more difficult to overcome. But, in the process, knowledge is being gained about the nature of the difficulties, the ways in which they can be effectively tackled, and the interactions between agrarian reform and other aspects of development. This section presents some recently published materials which describe and assess the experiences in agrarian reform during the past decade in various parts of the world.

The first article is an effort to elaborate an economic theory of agrarian reform and to refute the criticism of some specialists that, however desirable such reforms may be for political or humanitarian reasons, they make little contribution to economic development as such and may actually impede it. The second analyzes the nature of agrarian reform problems in Latin America and the policies and programs needed for coping with them. Focusing specifically on individual countries, the two concluding articles describe the key features of the highly effective agrarian reform in Taiwan, and the rather indirect and unexpected ways in which some significant progress has been made in Colombia.

THE CONTRIBUTION OF LAND REFORMS
TO AGRICULTURAL DEVELOPMENT:
AN ANALYTICAL FRAMEWORK

Philip M. Raup

[From Economic Development and Cultural Change, Research Center for Economic Development and Cultural Change; Chicago, University of Chicago Press, Volume XII, Number 1, October 1963, US$1.75, pp. 1-21.]

These are excerpts from the article.

The increasing attention to problems of economic development has been paralleled by a refocusing of attention on barriers to this development that are centered in land tenure structures. However, this reorientation of interest has thrown into sharp relief the lack of a body of theory to guide economic analysis [of land reform]. There is no shortage of partial theories or of rigidly held dogmas that pass for theory. But there is an acute shortage of comprehensive studies that draw together the experiences of many countries and areas into an articulated framework.

It will be argued in this paper that land reform concerns the formation and reshaping of attitudes and motivations that lie at the roots of economic behavior. Where similar attitudes or influences are involved in theories of saving or investment, there are no doubts about the "economic" nature of the issue. It is instructive to speculate on the reasons why these doubts arise when land reform is involved.

A primary reason for hesitancy is the general unwillingness of economists to take into account the broad

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organizational and structural frameworks within which economic activity occurs. In the past, available theories of economic behavior have emerged from the systematic study of firms and individuals. Built into these theories is a strong tendency to hold the institutional framework stable in order that analysis of the response of firms and individuals to economic stimuli can be reduced to manageable proportions. However, the predominantly static nature of most past economic theory is now generally recognized. In recent decades, this recognition has led to the formulation of an impressive body of theory under the general heading of economic dynamics. Dynamics, in this setting, typically means the introduction of time into the analysis -- time in which consumer tastes alter, technologies change, and depreciation schedules are revised in the light of experience.

Nonetheless, much current "dynamic" as well as "static" economic analysis is practiced within a static institutional framework. One feature of the land reform issue is that it cannot be considered without questioning the basic structural characteristics of the economy. It compels a dynamic treatment of the total economic framework as an organism subject to change. For some economists, the solution has been to invite the sociologists, social psychologists, political scientists, and philosophers to take over. The alternative proposed in this paper is that, as economists, we should re-examine our theories and explore the extent to which the land reform issue can be brought within an analytical framework of economic study.

Some Definitions

In the broad sense used in this paper, the concept of land reform refers to the full range of measures that may or should be taken to improve the structure or relations among men with respect to their rights in land. The term can then be paraphrased as "land tenure reform," and is here used to include the following types of reform:

(1) Measures directly involving the tenure under which land is held.

- (a) Promotion of ownership by the operator and the reduction of absentee landlordism.
- (b) Regulation of rental rates and practices, and the enactment of lease protection laws.
- (c) Consolidation into efficient-sized units of strip parcels and scattered holdings.
- (d) Subdivision of large holdings.

(e) Control of land inheritance to prevent excessive subdivision of holdings, or to discourage the accumulation of large holdings.

(f) Improvement of land surveys and systems of title registration.

(2) Related measures essential to the success of land tenure improvements.

(a) Development of an effective agricultural extension service.

(b) Improvement in commercial and cooperative marketing systems when the structure of land ownership dominates or restricts the market outlets.

c) Improvement in the conditions of agricultural labor under tenure systems in which land ownership includes some claim to the services of people living on the land.

(d) Improvement in the agricultural credit structure when inadequate credit is a barrier to tenure reform.

(e) Improvement in the arrangements under which land is bought and sold.

(f) Reform in land tax and fiscal policies.

Background and Setting

The basic importance of agriculture to economic growth is often obscured. With transitory exceptions, the food supply is not currently a barrier to further economic growth in the more developed nations. Problems of the food component in labor costs remain, with consequent foreign exchange and terms-of-trade difficulties. But, the current good health of the agricultural economies of the more developed nations, coupled with localized problems of agricultural surpluses, have made it difficult to reconstruct the contributions that agriculture can make in the early stages of growth.

This difficulty can be seen most clearly in prescriptions that call for the movement of labor resources out of agriculture. At appropriate stages in the development process, this is commendable advice. Its feasibility increases as industry develops and as realistic opportunities emerge for non-farm employment. However, for many presently underdeveloped countries and regions, it is an unrealistic goal.

The setting within which land reforms must be analyzed is provided by recognition that agriculture must furnish employment for large populations of underdeveloped countries. But this recognition alone is not

enough. In contrast to the "developed country" prescription that labor be moved out of agriculture, the opposite situation has emerged in some regions of Africa, Asia and Latin America. Rapid urbanization in these areas has created large pools of underemployed labor, predominantly in urban places. In terms of realistic development potentials, a goal of moving people solidly into agriculture seems indicated.

Processes of Agricultural Capital Formation -- The Private Sector

The agriculturist's interest in land reforms derives from the desire of rural peoples for the achievement of full operational and managerial potentials. The economist's interest in land reforms focuses sharply on the central issue of capital formation.

A clear understanding of the capital-forming processes that lead to agricultural growth is essential. In the early stages of agricultural development, this process is predominantly one of accretionary gains in capital stocks. The investment decisions involved are typically made in small segments, spread over many seasons or gestation periods. The capital formed adds to impressive totals, but the process is characterized by many small, plodding steps. This relationship is obscured by the emphasis on large-scale, dramatic investment programs in much current economic development planning. The image of development projected by a hydroelectric dam or by a steel mill is misleading if applied to agriculture. Capital in farming is rarely concentrated, in a spatial sense, and its formation is heavily weighted by the time dimension. It accumulates by an incremental process that is best described as accretionary.

A nation's livestock herd is a good example. Increases in numbers and quality, slow improvements in feeding levels, better disease protection, and increases in rates of gain are all achievements in which time plays the important role. In early stages of agricultural development in Europe and North America, this gradual accretionary improvement in the livestock herd was a primary capital-forming process. It is still under way in areas shifting from reliance on cash crops to animal agriculture. Accretionary processes are also important in the stock of farm capital represented by buildings, fencing, water supplies, land clearing, ditching, drainage, and other acts of melioration, soil improvement, and conservation. Where tree or bush crops are important, the process of accretionary buildup is particularly prominent.

This excursion into history should remind us of the validity of two propositions:

(1) Accretionary forms of agricultural capital formation are the important ones in early developmental phases, and in phases involving a shift from a cash-crop economy to a livestock-feed economy.

(2) The time spans required for effective operation of these accretionary processes are measured not in years but in generations.

One reason for this delayed response may be found in the time required for accretionary processes of capital formation to work themselves out. Where capital stocks are biological in nature, the limits within which capital-forming processes can be accelerated are relatively fixed. Agricultural policy for maximum growth in this development phase calls for the creation of patterns of production, consumption, and investment that maximize accretionary processes.

We can now state a major hypothesis that will guide the subsequent discussion: the land tenure system is a major force in maximizing accretionary formation of capital in agriculture and insuring that surpluses above sustenance levels are reinvested in the productive plant.

In exploring the significance of the hypothesis we should bear in mind how tenure security can contribute to capital formation. By making the use of a productive asset the preclusive right of an individual or a group, a situation is created in which the investor can realize upon his investment, in which the sower can reap where he has sown. This security of expectation is crucial for biological forms of capital, slow maturing enterprises, and undertakings involving numerous incremental additions made at successive intervals over many production cycles.

A system of tenure that makes these rights of use and reward specific to the user is a necessary although not a sufficient condition for capital formation to occur. The tenure must also be adequate, in terms of time and scale, to motivate the user to reinvest his surplus.

Within this framework of our general hypothesis, we are now ready to identify five additional propositions to guide analysis. We now hypothesize that the tenure arrangements under which productive resources are held and used will affect farm and farm family patterns of expenditures, savings, and investment in the following ways:

(1) By their influence upon the operator's time preference for money income.

(2) By their influence, over time, upon the allocation of expenditures between the farm firm and the farm household.

(3) By their influence upon the allocation of expenditures within the farm household as between goods and services for direct consumption and expenditures upon the family residence.

(4) By their influence upon disposition of the total available labor time of the farm family.

(5) By their influence upon attitudes toward and uses made of credit.

From the standpoint of capital formation, the first important characteristic of the small proprietary or family farm lies in the fact that every act of consumption in the household requires a decision not to invest in the productive enterprise. Operation within this consumption-investment matrix is calculated in two different units of measurement: (a) the allocation of money income, and (b) the allocation of family labor time. In terms of money income, and where tenure security is at a maximum, the operator can afford to balance the alternatives of maximum return over time from slow maturing investments against possibly lower yielding but quick-turnover investments. He can rationally afford to undertake investments whose yield may not reach a maximum in his lifetime. He can also afford to balance appreciation in value of his capital assets against enjoyment of realized periodic income. In short, a maximum incentive situation is created in which the growth of investments can be weighed heavily when balancing them against annual yield.

In the terms of the disposition of family labor, the prospects of long and secure tenure may create a condition in which the maximum incentive is given for the investment of total available labor time in productive undertakings. Much of agricultural capital formation can be explained in this fashion. Livestock care, repair and maintenance of structures, improved water supplies, drainage, soil improving practices, and a variety of similar tasks are often accomplished in agriculture at the expense of what might validly be regarded as leisure time.

To appreciate fully the implications of this argument, it should be recognized that leisure time in agriculture takes three forms:

(1) Enforced leisure, resulting from too few accessible productive resources with which to work. Unavailable capital and preclusively occupied land are the hallmarks of an agricultural economy exhibiting this trait. In this situation, the economist speaks of a zero opportunity cost for labor; the demographer speaks of overpopulation

(2) Cyclical leisure, resulting from one of three types of causes:

   (a) The biological nature of agricultural production, with its processes geared to crop seasons and gestation periods.

   (b) Weather and other natural hazards.

   (c) Price and market fluctuations of the economic cycle.

(3) Volitional leisure or "leisure by choice." This terms implies that some form of work could be performed. To the individual

agriculturist, the opportunity cost of this leisure is not zero, although his marginal productivity if he chooses to work may be nearly so. This is the situation that conventional economic theory assumes to be the norm.

The land tenure structure exercises a powerful influence on the disposition of leisure time in each of these three situations. Where agricultural labor is redundant because of physical shortages of working capital, the task of the tenure system is to put people to work. In this setting, proposals for land distribution programs assume their most persuasive form. The prospect that subsequent economic development may create nonfarm employment opportunities has led many economists to condemn land distribution programs because of the "uneconomic" size of farm units that may result. In the long run, this argument may have validity. In the shorter run, the waste of capital-forming potential represented by underutilized labor is more serious. In this sense the political pressures leading to drastic land reform programs may also be good economics.

Where leisure has a price and choices can be made, the capital-forming potentials of land reforms are of increasing importance. This situation enhances the significance of the creation of economic incentives because defects in tenure arrangements can be most costly in terms of inhibited economic growth.

These incentive conditions can be created by a tenure system, but there is no guarantee that they will be used. The scale of farm operations is often too small, and the balance of enterprises inadequate. Or, the cultural and motivational patterns that might lead to these investment forms may be lacking.

The biological nature of agricultural production introduces a dimension that bears heavily on these patterns of investment of family labor. Much of the "cost" of agricultural production is a time cost. Crops must ripen, animals must mature, and a principal part of the labor cost of these processes is the cost of waiting. Even on well-organized farms, there are substantial time periods in which the labor force must be on hand but technically underemployed. A key to the processes of agricultural capital formation lies in the use made of this periodically available labor. In terms of capital creation, that pattern is best which creates the maximum likelihood that the farm family will elect to "exploit" its own labor.

Basic to this argument is the expectation of a long-term rise in real incomes. Where incomes are falling or are uncertain, household-consumption versus farm-investment decisions have repeatedly been resolved in favor of the maintenance of family consumption levels. When income falls, existing levels of living tend to be maintained -- at the

expense of unrewarded depreciation or ultimate exhaustion of land and capital. The capital-creating combination of secure tenure and expectations of rising real income has its antithesis in the form of unrealistically high consumption goals coupled with the prospect of falling real income.

The generation of new attitudes toward debt and credit is another major contribution that land reforms can make to capital formation. Tabus against debt are characteristic of tradition-bound agrarian societies. The tabu has not prevented debt, but it traces from and tends to preserve attitudes that confine the use of credit to consumption purposes.

The emergence of concepts that relate debt repayment ability to increased output is one important prerequisite for agricultural development. It is in this regard that land reforms, properly conceived and executed, can make decisive contributions. Where land has been received through land reform, the development of payment schedules based on the income-yielding potential of the land can introduce the concept of amortization. More importantly, it can provide a vehicle for supervised production credit under conditions that make supervision acceptable to the farmer.

The development of workable schemes for supervised credit has been a prominent feature of successful land reforms. Without this feature, land reform can become little more than an episodic redistribution of wealth, shorn of the dynamic influence that credit can introduce. New incentives to invest family labor may be of little value if the agriculturist has no new tools and processes with which to work. A secure tenure in land can lead to stagnation if it is not coupled with attitudes and institutions that will make production credit available and encourage farmers to use it. In this sense, emphasis upon extension services and credit supervision acquires a dominant position.

These optimum conditions for capital formation in agriculture have been presented in terms of the owner-operated farm, but this is not the only tenure arrangement that can create these conditions. It is possible to devise leasing arrangements that will create security of expectations, specific to the operator, and for a period of time long enough to encourage long-term investment. However, the representative lease in underdeveloped agricultural areas is some form of a short-term share lease. Let us examine the implication of this tenure form for capital-forming processes. If land and buildings are provided by the landlord, with tenant contributions limited to labor, livestock, and equipment, the tenant has an incentive to invest in livestock and equipment but not in land improvements or structures. He has little or no incentive to devote income or leisure time to the gradual improvement or maintenance of the real property assets. Because of the

importance of capital investments in farm buildings for some forms of animal agriculture, this system has prevented or delayed a shift from a cash-crop to a livestock-feed form of agricultural enterprise.

Where this weak incentive situation is associated with a heavily skewed pattern of income distribution and a prominent "demonstration effect" of conspicuous consumption by a social elite, we have a minimizing condition for capital creation. Economic arrangements limit the incentive for investment and the cultural setting maximizes the incentive for consumption.

Processes of Agricultural Capital Formation -- The Public Sector

Alfred Marshall, and the generation of economists that he trained, contributed to economic theory the concept of external economies of scale. The concept was crucial to further development of the theory of the firm. It provided the framework needed to accommodate those aspects of economic behavior and development that could not be explained by conventional tools of microanalysis. In a similar vein, the analysis of capital-forming processes in agriculture is incomplete if it is confined to the behavior of farm families and individuals in their private role as entrepreneurs. Recognition of this fact is widespread in recent literature on economic development, and a new terminology has emerged. We speak of social overhead capital, of the economic infrastructure, and of contributions to growth that follow from investments of public capital in activities that would be unprofitable if undertaken by private firms.

The image evoked by this terminology is typically of physical, tangible goods: hospitals, power dams, irrigation systems, port facilities, and (in the majority of countries) the entire road, rail, air, and wire system of transport and communications. Of no less importance are the intangible forms of this public capital represented by systems of public health, education, local government, and community organization. It is for these latter forms of public capital, represented by institutions and organizations, that the land tenure system of a country is of great importance.

As governments grow in their capacity to govern and as taxpayers mature in their understanding of the benefits of public capital formation, the identification between taxpayer and beneficiary is typically relaxed. Heavy public investments in education and training are supported in developed countries by individuals who cannot conceivably be reckoned among the direct beneficiaries. Where the land tenure structure will support a companion land tax structure, an incentive situation is created within which the almost universal human desire to see one's children prosper can begin to work. Rural education in underdeveloped regions emerges as one form of public capital investment for which taxpayer support can be most readily mobilized.

In addition to increased tax revenue, land reforms have typically brought a train of events leading to important secondary benefits to the social overhead capital structure. One clear example is improvement in systems of cadastral survey and land title registry. The absence of accurate surveys has been a severe handicap to economic development in many underdeveloped countries. Inability to establish a legally defensible title to land restricts the development of mortgage credit. Settlement is inhibited, and wasteful disputes over boundary rights are frequent. The cost of a cadastral survey in time and money has been one stumbling block in many land reform programs, but this difficulty should not blind us to the ultimate result. Where these surveys are lacking, they are a prominent measure of a nation's poverty. The costs of overcoming this defect are so high that they must typically be spread over several generations. For these reasons the early construction of survey and land title registry systems is high on the list of prescriptions for agricultural development. A tenure structure that contributes to this goal can exercise an undramatic but long-lasting influence over the course of a nation's growth.

A related form of public capital investment in agriculture concerns the data systems through which agricultural statistics are assembled. Rational economic behavior is a function of the quality of information at hand. The growth of data-collecting systems can be helped or hindered by the nature of the country's land tenure structure and the relations it engenders between rural people and their governments.

Where the tax collector is the primary contact between rural people and government, the suspicion with which he is traditionally regarded extends to all government representatives. An effective agricultural education and extension service finds this an inhospitable climate in which to grow. The collection and interpretation of agricultural data from farm operators becomes an exercise in subjective bias estimation. Where land users have secure possession of their land they can project their long-run interest in the accuracy of reported data. This interest-base is typically lacking in areas of insecure tenures in land, absentee ownership, or layered tenancy. Self-reporting techniques are unreliable and the investment of public capital in better data is stunted or yields a low return.

Another form of social overhead capital in agriculture comprises the structure of marketing institutions available at the farm and village level. Insecure tenure in land, not specific to an individual, plus small and fragmented units, may make it difficult to promote effective market or distribution systems in many backward and agrarian regions. Small-scale and localized monopoly is the rule with the landlord often performing the related functions of creditor and local market outlet. In this setting, the development of efficient commercial or cooperative marketing and credit facilities should accompany changes in the tenure system.

This list of the forms of social overhead capital in agriculture that are strongly influenced by the land tenure structure might well have included water supply, irrigation, local roads, police protection, accessible civil justice, and community recreation facilities. Enough has been said to emphasize that the cost of providing these services is a heavy burden on the net capital-forming capacity of underdeveloped areas. Land tenure structures can inhibit or promote the assumption of this burden by local people. Where these services must be provided by the central government, costs are higher and government loses an essential element of identification with the hopes and aspirations of the people served.

The Significance of Land Reforms in Creating Incentives for Increased Output

The discussion to this point has been focused upon the nature of agricultural capital and the processes of its creation. If we accept the general argument that land tenure structures condition the investment process in agriculture, we must then ask: how may land tenure reforms contribute to the increased agricultural output that is required before there can be any surplus to invest?

We must recognize that one criterion of economic thought is a belief in the potential economies of large-scale production. This is paralleled by a preoccupation with output per man hour as an appropriate measure of productive efficiency. These twin articles of faith have strongly influenced conventional economic thinking about land reform.

With this in mind, let us examine the course of technological development in the agricultural economies of more developed countries. It will be useful to classify technological development in terms of changes in production techniques that are (a) labor saving, or (b) output increasing.

In some sparsely settled underdeveloped countries -- areas of Latin America, Africa, and the Middle East -- the pressures are likely to be wage-induced and hence technological advance takes the form of labor saving. Where population pressures are high, the incentives for advance arise from the compulsion to develop substitutes for land and to adopt output-increasing technologies.

In these situations, the incentives needed are those leading to better seed selection, heavier rates of fertilization, improved land management and animal husbandry practices, and the selective use of agricultural chemicals. Some aspects of output-increasing technologies can be introduced by a relatively small number of trained people, strategically located. Artificial insemination and improved seed breeding illustrate the point.

The majority of output-increasing forms of agricultural technology depend on an improvement of the technical skills and management capacity of virtually the entire farm labor force. Fertilizers, chemical weed controls, pesticides, and improved animal feeding practices are examples. The land tenure reform that will best serve these needs is one that will give the maximum incentive for increased output to the largest percentage of the agricultural labor force. Large-scale, heavily mechanized units do not seem suited to this task. Small-scale units, intensively worked by a literate and skilled labor force having a direct interest in high output and good husbandry, are the ones indicated.

The impact of land tenure structures upon the choice of technology is also apparent in irrigation agriculture. Economists have noted a tendency in underdeveloped countries to focus upon large dam and irrigation works while neglecting the development of fertilizer and agricultural chemical industries. In terms of increased food output, capital invested in water supply and irrigation would often yield a greater and a quicker return if devoted to fertilizer production. Why do poor countries continue to build big dams?

A part of the reason is that political leaders can point to tangible results and international credit agencies can rest assured their capital has gone into durable assets. Further explanation can also be found in the land tenure structure. In an agricultural economy characterized by several levels of subtenancy the cost of applying fertilizer or a new cultivation technique may fall heavily or entirely upon the tenant. He may understandably be reluctant to add this risk and expense. Traditions with respect to water rights, however, are often strongly influenced by egalitarian customs of "equal rights." The distribution of rights in water may be more nearly in proportion to the tenant's share in marginal costs. Defective land tenure arrangements thus provide a clue to the reason why "use more fertilizer" campaigns have met with limited success in many underdeveloped regions.

The improvement of product quality offers an additional and significant opportunity for land tenure reforms to affect a nation's agricultural output. Where land reforms have been accompanied by the development of strong producer cooperatives, the producer's pride in his farm could be coupled with market pressures for product quality improvement. Difficulties in securing farm products of uniform and high quality from a multitude of small peasant-type producers have led some economists to conclude that the task is impossible in many underdeveloped countries. Attention has shifted to estate and plantation-type units or to variations of large-scale collective-type forms of farm organization.

These centrally directed units can organize masses of unskilled rural labor into reasonably efficient production cadres. In backward

areas where managerial talent is scarce, these units economize on management. There are thus strong reasons why they have tended to emerge early in the histories of agricultural development of a wide variety of countries, including the United States, India, and the Soviet Union. Plantations or collective farms conserve scarce managerial skills, permit labor supervision on a mass basis, and make possible the achievement of acceptable levels of product quality and standardization. These are impressive short-run accomplishments.

But these gains have been acquired at a high price in many countries. Plantations and other large-scale units have seldom contributed to the development of quality in the human labor resource. And, they have conspicuously failed to promote the development of intensive animal agriculture. By inhibiting the development of widespread networks of agricultural education, extension, credit, and marketing services they have perpetuated an agricultural structure made up of a small, modern sector using high skills, and a large primitive sector of native production.

One body of economic theory in agriculture holds that the question of size of farm and the land tenure system appropriate to its support is predominantly a technical one. This reasoning typically includes an implied assumption of decreasing costs or increasing returns to scale. It is generally invoked to protest land reform programs that threaten to create uneconomically small units.

As our understanding grows of the functioning of economic systems in a variety of cultural settings it is increasingly common to find recognition of the fact that, in Hirschman's phrase: "Minimum economic size is not a technical concept, but is defined in economic terms relative to normal profits and efficient foreign suppliers." This is a step forward in the application of theory, but it still does not bring us to the central issue. The "economic" size of the farm is not only an economic concept -- it is a cultural concept as well. It cannot be interpreted without reference to the total setting in which economic activity occurs.

One characteristic of output-increasing technologies in agriculture is that many of the most important ones are divisible -- they are technically capable of application in small "doses." Fertilizers, better seeds, agricultural chemicals, and improved animal feeds and feeding practices are examples. It may be granted that small farms can apply this technology effectively, but it is then often argued that they cannot meet the quality standards demanded in export markets or offered by competing imports.

Where this argument has merit it will often be found to have its roots in a defective land tenure structure. In this sense, land tenure

reforms can promote qualitative as well as quantitative improvement in agricultural production and in the human skills and abilities on which increased productivity must ultimately rest.

Conclusions

Much discussion surrounding the issue of land reform and economic development is presented with a negative cast. Defects in land tenure appear as an obstacle to development; the issue is resolved when the obstacle is removed.

This paper emphasized the view that land reforms may contribute to economic development not by removing obstacles but by promoting a new climate of expectations. The stress here is on the creative act of devising a new basis for the identification of reward with effort, of balancing costs against returns. Land reform can be a sterile and debilitating experience if carried out in a narrow setting, without the support of other reforms in systems of education, extension, credit, and taxation. It can build upon or it can dissipate the political strength inherent in programs that can generate high levels of emotion and national effort. Whether or not these potentials are realized depends heavily on the extent to which political and social demands for land reform can be supplemented with economic analysis.

We have argued that accretionary types of capital are typically needed in the agriculture of underdeveloped countries. Capital formation in this setting may depend less on large-scale injections of money capital into agriculture than upon changes in attitudes and the institutional structures they support. From this point of view, a premium attaches to the land tenure structure that can create incentives for rates of output expansion that will run ahead of consumption and will promote investment of the surplus in superior productive processes.

In some areas, economic development plans call for capital formation along these lines, using a variety of forms of coercion. Inflation, suppressed levels of consumption, mandatory product delivery quotas, artificially low fixed prices, and ultimate threats of physical violence are all in use. This paper reflects the view that production effects are maximized and social dislocations minimized when the agriculturist can be attracted to these same ends through opportunity instead of coercion. The primary task of land tenure policy is to create conditions that permit opportunity motives to operate. No forms of "exploitation" are so effective as the ones we impose upon ourselves.

POLICIES AND PROBLEMS OF AGRARIAN REFORM
IN LATIN AMERICA

[From 1963 Report on the World Social Situation; Department of Economic and Social Affairs, United Nations, New York, 1963, Sales No.: 63.IV.4, US$2.50; pp. 129-137.]

[In 1963, the United Nations initiated a new series of reports on the world social situation, to be issued biennially. The first Report contains statistics on and analysis of the world trends in population; health conditions; food and nutrition; housing, building, and urban and regional planning; education; manpower and employment; labor -- income, working conditions, and relations with employers; social security systems; and social development programs. Chapters devoted to Latin America, the Middle East, Asia, and Africa survey in greater detail the developments in these fields and the changes in social structures and relationships in rural and urban areas that have occurred in recent years.

These excerpts are from the chapter on social development in Latin America.]

These are excerpts from the report.

Up to the present, three Latin American countries have carried through agrarian reforms that have changed the ways of life of the majority of their rural people: Mexico, in a process that has continued for nearly forty years and is still evolving; Bolivia since 1953; and Cuba since 1959. A fourth country, Venezuela, is in the midst of a reform that is intended to be as far-reaching as its predecessors. A fifth, Guatemala, embarked upon an ambitious agrarian reform programme in 1952; this was for the most part abandoned after the revolution of 1954, but has had an impact on the rural population that cannot yet be assessed. Colombia enacted a comprehensive agrarian reform law in 1961; Chile, Honduras and Peru did so in 1962; at least four countries (Brazil, Ecuador,

Nicaragua, and Panama) have draft laws in various stages of preparation or discussion by their legislative bodies.

Most of the Latin American countries already have laws of more limited scope providing for distribution of public lands and, in some cases, for expropriation of unused private lands. Many of them have created commissions or institutes of agrarian reform, usually as semi-autonomous public bodies. The newer legislation is generally both comprehensive and complicated; this stems both from the efforts of special interests to protect themselves and from the aspiration to take full advantage of the lessons of earlier reforms and deal with the rural problem in an integrated way.

Both the reforms that are now in progress and the draft laws envisage some combination of the following policies:

Colonization and Resettlement

Colonization of vacant lands is usually one of the first practical measures to be undertaken -- often long before it is presented as one element in agrarian reform. The over-crowding of many of the older agricultural areas under existing conditions of tenure and production techniques and the availability of huge areas of empty land make colonization an essential part of rural policy in most Latin American countries. However, colonization schemes are over-emphasized by some sectors of opinion and looked on with suspicion by others because they do not involved interference with present tenure arrangements and are not resisted by large landowners.

It is probable that in most Latin American countries, the opening of new lands will have more immediate importance as a means of increasing agricultural production than as a means of meeting the land hunger of the rural workers. The opening of new lands for commercial farming requires very heavy investment in roads, clearing of forests, building of houses and schools, and provision of health services to combat tropical diseases. It also requires experimentation and instruction in new agricultural techniques. The men best fitted to pioneer in such areas are those with experience of commercial farming, and with capital to meet at least part of their needs until the farm becomes productive. Countries such as Brazil and Venezuela have in the past followed this reasoning by trying to secure for colonization projects immigrants from Europe or Japan rather than local cultivators. For the same reason, some of the reform projects envisage optional compensation in the form of vacant land for landowners whose holdings are expropriated since, it is hoped, they will have capital and initiative to exploit such land.

However, most of the national agrarian reform policies also envisage the planned resettlement of small cultivators, under supervision

and with fairly elaborate agricultural and social services. The few experiments that have been made indicate that such colonies are slow to succeed and expensive in relation to the populations involved.

While organized resettlement of small cultivators is thus still at the stage of pilot projects, a great deal of spontaneous resettlement is going on without any cognizance, help or control from official agencies. The movement has been on a much smaller scale than the cityward migration, and only guesses can be made as to the numbers involved, but it affects some of the rural groups reputed to be most conservative. Andean Indians are moving down the eastern slopes of the mountains into the sub-tropical river valleys. About 5,000 families are believed to have settled in the Tambopata Valley of Peru over the past 30 years, and the Government expects a flood of migrants with completion of a road into the area around 1963; 40,000 to 50,000 Indians are believed to have moved spontaneously into the Bolivian lowlands over the past 15 years. Meanwhile, Brazilian, Colombian, and Central American peasants have been drifting into new areas of settlement. Such migration often precedes the construction of roads but rises rapidly as the roads are extended. The partial conquest of malaria, which previously made some of the valleys almost uninhabitable, has removed one of the most important barriers to resettlement.

Such a movement has both promising and ominous aspects. On the one hand, it goes far to disprove opinions formerly advanced to the effect that highland peasants could not adapt themselves to tropical settlement for both physical and psychological reasons. On the other hand, it threatens an extension of the minifundio patterns since the settlers clear only the small plots they can cultivate with hand implements, have only limited access to markets, and live so thinly scattered that it will be hard to bring schools and health services to them. At the same time, it means an enormous waste of forest resources through slash-and-burn cultivation, and much of the land now being cleared may eventually be left eroded and worthless. In Brazil, where penetration of the interior has not been deterred by abrupt changes in altitude and climate, this process has gone on for a long time, leaving a "hollow frontier"; that is, much of the land near the coast has been exhausted and abandoned, and urban food supplies come from newly cleared areas hundreds of kilometres distant from the coastal cities. Another unfortunate aspect of the penetration of parts of the interior of South America is the continuing displacement of previously isolated Indian tribes by the new settlers, usually without any effective intervention from the distant national authorities. Nonetheless, these countries may find the provision of guidance and assistance to spontaneous resettlement more effective than the more formal colonization projects on which they have concentrated.

Land Tenure Reform

The reform of tenure in the older agricultural regions is the most controversial aspect of rural policy, and its unanimous endorsement by the Latin American Governments in the Punta del Este Charter sums up one of the most remarkable changes in recent years. The reasons for this change have been mixed, and the practical results vary widely.

The high degree of concentration of landholdings in Latin America, probably exceeding that in any other major region, is well known and illustrative statistics can be found in a number of sources. The following table summarizes the situation around 1950 for the region.

Size of Farms (Hectares)	Percentage of Farms	Percentage of Land Area
0-20	72.6	3.7
20-100	18.0	8.4
100-1,000	7.9	23.0
Over 1,000	1.5	64.9
Total	100.0	100.0

In general, the very small holdings (*minifundios*) are intensively cultivated, but can hardly afford their owners subsistence, let alone a surplus for the market. The cultivators' primitive techniques and their inability to give their land fertilizer or adequate rest from cropping mean inevitable soil depletion and declining ability of the *minifundio* lands to support even their present population. The very large holdings (*latifundios*) are not intensively cultivated and include large areas of land held idle for speculative purposes. The reform policies envisage a combined attack on the two extremes. The *latifundios* are to be induced or compelled to give up part of their land and to farm the remainder more efficiently, while the *minifundio* cultivators are to receive holdings large enough to enable them to function as efficient family farmers. The two problems that arise immediately are the financing of land expropriation and the transformation of subsistence cultivators into true farmers.

Land in most of the countries is over-valued in relation to the income that is derived from it, partly because of the traditional prestige of land ownership, partly because of its usefulness as a hedge against inflation. Government purchase of land voluntarily offered for sale is thus not practicable, and laws authorizing this method of acquiring land for distribution have been ineffective; where such sales have been made the landowners have simply unloaded their poorest land. The few countries that have carried out large-scale reforms through expropriation have all adopted systems of compensation unacceptable to the landowners and enforceable only after the latter had

lost all influence over government policy. These systems usually involve compensation in long-term bonds rather than in cash and at the low tax valuation of the land rather than the high market value. In several countries the constitutions require cash compensation; Brazil and Chile are now proposing constitutional amendments permitting compensation in bonds.

A more indirect method of changing the tenure system has been attractive in theory but ineffective in practice. A few countries, Colombia in particular, have provided for graduated land taxes with higher rates for idle or under-utilized land. It was hoped that such taxes would force the landowners either to sell part of their land or bring the whole into production. In practice, the Governments have lacked basic data and administrative machinery for enforcement of such laws.

In the case of the traditional large estates, there is no question that a transfer to family farming can increase production. The modern plantations producing export crops such as bananas and sugar present quite different problems. Here, operation of very large units, with ample capital and able to use heavy machinery efficiently, may be more productive than any alternative system. The main objections to the plantation system have derived from the plantations' extensive powers over their workers, the heavy seasonal unemployment associated with the system, and the concentration of production on one crop, to the neglect of food production. The permanent labour force enjoying full benefits of job security, housing, etc. may amount to less than half the labour force at peak seasons; many of the workers are employed only 80 to 100 days in the year. An adequate year-round livelihood for such workers cannot be found within the plantation system.

Problems of Minifundios

In most of Latin America, the dwarf holding (minifundio) has long co-existed with and supported the latifundio. The small cultivators with one or two hectares of poor hillside land have formed a convenient reserve of seasonal labour for the large estates occupying the fertile valleys, and even for distant mines and tropical plantations. The position of these cultivators has naturally tended to deteriorate as their holdings have been divided into even smaller plots through inheritance, as erosion and over-cropping have ruined fertility, and as the large estates have continually encroached on them through such devices as monopolization of water for irrigation. In many areas, also, seasonal work opportunities have declined with modernization of the estates. In Chile, minifundio owners are reported to have turned to petty trade, particularly the selling of alcoholic beverages to estate workers.

In the present reform policies, the elimination of minifundios is regarded as just as important and difficult as the breaking up of

latifundios. Fragmented holdings need to be consolidated, a good deal of eroded land needs to be retired from cultivation altogether, and some cultivators must find land or employment at long distances from their traditional homes. Most of the reform laws set standards, varying with type of land, for minimum size of economic holdings. On this point, however, national policies are ambivalent. Immediate social and political pressures conflict with the requirements of raising productivity, and there is a well-known danger that in practice the land reforms might increase the prevalence of *minifundios*. This has already occurred in the Mexican and Bolivian reforms and is threatened in Venezuela. In Chile and Peru the legal provisions for compulsory consolidation of dwarf holdings have given rise to natural fears that the reforms will be used to take from the poor the little land they have, and will be hard to enforce.

The most urgent demands for land distribution come from the most densely populated rural areas, in which there is not enough land to give each family a plot of economic size. Most of the beneficiaries, with their lack of capital and primitive techniques, cannot cultivate more than a subsistence holding. Also there is another reason why some of the land reform programmes contain separate provisions for the granting of very small holdings. The reforms commonly assume that large holdings requiring wage labour will continue to operate, as long as they are productively efficient and do not monopolize unused land. Ownership of a house and garden would give the rural worker some protection against the power associated with such large holdings, and a better opportunity for stable family life. Home ownership for rural workers is clearly a desirable objective, but careful planning and supplementary measures such as enforcement of minimum wage laws will be needed if the very small holdings are not to perpetuate the present relationship between *latifundios* and *minifundios*, in which the former can pay wages below subsistence level because the workers grow most of their own food.

The landless worker is found also in the few areas in which small farms predominate, and here he may be even worse off, since the small farmers need only occasional help, most of which they can obtain from their neighbours. A recent study of rural life in Costa Rica finds that the landless workers make up a distinct group at the bottom of the rural social scale. The working capacity of the men in this group is lowered by malnutrition and apathy; they are the last to be hired by local farmers for seasonal work. The cultivators with very small holdings in the same neighbourhoods are both more productive at such work and show more initiative at finding supplementary income outside farming (in particular, by illicit distilling). The landless workers are excluded from most community activities; because of their inability to contribute dependably to the support of a wife and children, their family life is more unstable than that of other groups in the community. Most of them are descended from several generations of workers in the same plight.

Weakness of Rural Community Organizations

The present rural policies envisage a social and political as well as an economic transformation in the countryside. The often-described rural passivity and neglect are no longer general, but in most of Latin America there are no satisfactory recognized channels through which the rural population can express its demands, through which tenure reforms can be adapted to local needs and desires, and through which the local population can join forces with the national agencies to make effective the services that are needed to complement tenure reforms.

This weakness or absence of rural community organization and the traditional tendency to disregard rural opinions introduce a serious danger that land reform and other rural programmes, whatever their stated principles, will continue to be managed from the top and distorted to serve the interests of groups that can reach the ear of authority -- whether the authorities in the national capitals, the politicized national leadership of peasant organizations, or the lowest echelon of government officials and the judges of land courts operating in the municipal capitals. Ideals of local self-government are not lacking in Latin America, and many advisers have persistently urged its strengthening.

Reforms of land tenure and rural community organization imply simultaneous improvements in rural education, health practices and housing, in the organization of production and marketing, and in the supply of credit.

Improving Rural Education

The Latin American countries, like many in other regions, have long relied heavily on the school as the main stimulus to change in the countryside. The geographical distribution of schools has gradually widened and rural enrollment increased, so that today the rural teacher is often the only public servant (aside from the policeman) who actually lives in the rural areas and has a continuing contact with rural people. The typical shortcomings of the rural schools, however, have not been overcome. The educational level of their teachers remains very low; and the typical school curriculum, specified to the pettiest details in national regulations, is quite unrelated to the capacity of the teacher, to the time the children will spend in school, or to the rural environment. Most rural children pass through only one or two grades of schooling, not enough to secure functional literacy; in fact, most of the rural schools do not offer a complete primary course, defined as six grades in the majority of countries. Teachers working under such conditions have sometimes been called upon in national programmes to organize adult literacy classes, promote better community health habits, and even provide agricultural advice; the results have naturally been limited.

Programmes of research and experimental pilot projects seeking methods by which the rural teacher can meet the heavy responsibilities placed on him are now found throughout Latin America. Rural normal schools and arrangements for in-service training of rural teachers have been created. Several countries have introduced nuclear school systems, in which a central team of specialists, including a social worker and public health worker, aids several teachers in scattered one-room schools, and the children have an opportunity to complete their primary education at a central school. Educators are also pointing to the practicability of complete primary courses in one-teacher schools, on condition that the regulations are made more flexible and the teachers given adequate guidance. In most countries, the new methods have as yet benefited only a handful of rural children; the difficult next step is to find (and pay) enough dedicated teachers and supporting specialists to move out of the pilot project stage.

The prospect of continuing movement of youth from farms to cities strengthens the rural demand for education but complicates the task of reforming its content. The school should not encourage the children to reject rural life, as it is often accused of doing; but a schooling narrowly adapted to rural needs will only perpetuate the present handicap placed on rural youth who must compete for urban jobs and adapt themselves to urban ways of life.

The need is not only to raise the general educational level of the rural population but also to enable qualified rural youth to reach the higher rungs of the educational ladder, and to do this in such a way that an adequate proportion will return to provide leadership and technical guidance to the rural masses. Up to the present, rural youth have been almost entirely excluded from secondary and higher education by the incompleteness of the primary courses offered in rural schools; the exceptions have naturally entered urban occupations. Agricultural education at the secondary level has been offered only on a very small scale, and the few institutions of this type have been sparsely attended; such education was incompatible with the social structure in the countryside. The larger landowners were not interested in such an education for their children and the rest of the rural population either could not qualify to enter or saw no advantage in doing so.

Agricultural education at the university level naturally shows similar weaknesses. While government agricultural agencies have devoted considerable effort to the creation of faculties and institutions, enrollment in them averages only 57 per cent of capacity, while most other branches of higher education are over-crowded. In 13 countries in 1958, enrollment in agricultural courses ranged between 6.0 per cent and 0.4 per cent of total higher enrollment, for an unweighted average of 3.1 per cent. A large majority of these students come from the urban middle classes and try to find work in the cities after graduation, especially in the central offices of government agricultural agencies. Meanwhile,

the region is equally short of qualified agricultural extension workers and of the detailed information on local soil types, plants, insect pests and many other matters needed for a sound agricultural policy. These deficiencies, in countries of remarkable topographic and climatic diversity are bound to cause unnecessary waste and disillusionment once large-scale resettlement is undertaken. Such questions of technical assistance fall outside the scope of this analysis, but their importance cannot be over-estimated. The numerous agricultural specialists needed for present rural plans can be obtained -- and persuaded to go where they are most needed only -- if the educational opportunities of rural youth at the primary and secondary level are greatly improved.

Other Rural Needs

The inter-connected rural deficiencies in education, economic opportunities, and institutions for collective action have limited the effectiveness of a number of other rural programmes that are receiving a new impetus from the imminence of agrarian reform.

Several governments have promoted rural co-operatives over a number of years. The inefficiency of the present urban marketing systems and the hardships worked on the small cultivator by his inability to hold his crop off the market to wait for a favourable price indicate their potential value. Successful co-operatives, however, imply competent and dedicated advisers, local officers with some education, and a certain amount of mutual trust and disposition to co-operate. The lack of these prerequisites in much of Latin America has prevented rural co-operatives from attaining a mass membership.

Farm credit institutions in most of Latin America have served only the larger landowners. Even the few public credit institutions specifically designed to meet the needs of smaller farmers have not been able to reach the *minifundio* cultivators. The Mexican Banco de Crédito Ejidal, for example, set up to assist the beneficiaries of land reform, after many years of operation, by 1959 extended credit to only about a quarter of the *ejidos* -- the more prosperous among them. In fact, even if funds were ample and the administrative difficulties of lending money to persons with minute and precarious cash incomes, who are also illiterate and remote from the lending agencies, could be overcome, the small cultivators are more likely to use credits for non-economic purposes than to increase their production.

The supervised credit system initiated in Brazil in 1949 and since extended on an experimental basis, usually with the support of funds from abroad, to a number of other countries, is designed to overcome these difficulties. Under this system, credit is supplied to selected cultivators who agree to follow a production plan. The beneficiaries receive assistance in improvement of home life as well as in agricultural

practices and marketing. The costs of such a method, in terms of trained supervisory personnel, are too high for it to be applied to very large numbers of farmers, and its proponents rely partly on the "demonstration effect." That is, it is hoped that the success of the first beneficiaries will stimulate their neighbours to imitate them, and that gradually it will be possible to extend loans with less supervision. The method is still in process of evolution and experiment, as its promoters attempt to broaden its influence at lower costs per beneficiary. Some programmes combine more limited supervision by technicians with the organization of local committees of cultivators to administer funds, decide on loan applications, and see that the loans are used for their stated purpose. A recent report by the ECLA/FAO Joint Agricultural Division comments: "By its very nature, 'supervised credit' is costly. But as the importance of its educational and formative aspects is appreciable, the educational costs of credit should be set apart, so that they are imputed not to the loan, but to special items in the national budget or to international funds that might be earmarked for this purpose."

LAND REFORM IN TAIWAN, REPUBLIC OF CHINA

Jen-lung Chen

[From "Land Reform in Taiwan, Republic of China," a paper prepared for the United Nations Conference on the Application of Science and Technology for the Benefit of the Less Developed Areas; (Agenda Item C.1.1--E/Conf.39/C/190, Oct. 1962), United Nations, New York, N.Y.]

These are excerpts from the paper.

Since 1949, the National Government of the Republic of China has introduced a series of land reform programs in the rural areas of Taiwan. These reforms have resulted in remarkable improvements in the social and economic conditions of more than one-half of the entire population on Taiwan.

Taiwan, a sub-tropical island lying off the southeastern coast of the Chinese mainland, is predominantly agricultural with a land area of 35,961 square kilometers and a population of almost 12 millions. While about 900,000 chia (one chia equals 0.9699 hectare or 2.3968 acres) or one-fourth of its total area are cultivated lands, 5.3 millions or 50% of its total population are farmers. Of this 900,000 chia, 60% are paddy fields for growing rice and 40% are dry lands for growing sweet potato, sugarcane, tea, pineapple, jute, peanut and citrus fruit. Rice and sugar are the two major farm products on the island. In 1961, it produced 2.1 million metric tons of rice and 920,000 metric tons of refined sugar.

Agriculture in Taiwan is operated on small holdings. On its 900,000 chia of farm lands, there are 785,592

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farm families with each family tilling an average farm of only 1.2 chia. Those who till farms smaller than two chia form 88% of the farm families. When land reform was first introduced in 1949, the total cultivated land, excluding 180,000 chia owned by the Government, was distributed among 610,000 private owners of whom 170,000 were landlords. Before the introduction of land reform there were 39% tenant farmers, 25% part-owners and 36% owner-cultivators. But more than 41% of the cultivated land was under tenant operation.

The conditions under which farm lands were leased on the island before the reform were unfavorable to the tenants. Rents were at least 50% of the crop harvest. In addition, tenants had to furnish their own fertilizers, farm equipment and farm buildings. To lease land they had to pay "key money" and to keep it they had to renew the lease each year. These factors, together with the small acreage they cultivated, had made it extremely difficult for them to earn a decent living. The results of such a situation were discontent and unrest in the rural areas.

To correct this situation, the Chinese Government instituted a series of land reform programs with the technical and financial assistance of the Chinese-American Joint Commission on Rural Reconstruction. These programs were started in 1949 and completed in 1953.

Farm Rent Reduction Program

The first was the farm rent reduction program. It was enforced on the island in 1949. Its important features are as follows:

(a) Limitation of farm rent: To reduce the rent, all paddy fields and dry lands were classified into 26 grades and a standard yield was fixed for each. Then, the new rental rate was set at no more than 37.5% of the standard yield, regardless of the amount actually harvested. The reduction was effected by means of a new lease contract between the landlord and his tenant and registered with the Government.

(b) Protection of tenant's right: First, tenure of lease was lengthened to six years beginning from 1949. Second, key money was abolished. Third, advance payment of rent was prohibited and the amount of rent at 37.5% rate, its kind, purity, date and place of payment were all clearly stipulated in the lease contract. Finally, conclusion of new lease contracts and revision and termination of existing lease contracts were duly registered with the Government. All these provisions were strictly enforced by the government supervisors.

(c) Establishment of farm tenancy committees: To give additional protection to tenants against illegal acts by unscrupulous landlords, the Government encouraged farmers' participation in the program execution by creating a farm tenancy committee in each township and district to mediate and settle rent and lease disputes. The committee membership

included tenants, owner-cultivators, and landlords but gave tenants a greater voice in dealing with rent reduction matters.

Sale of Public Lands Program

After the rent reduction program was carried out on 260,000 chia of private tenanted lands, the Government started to sell the vast public lands on which a sizeable farm population was working as tenants and farm hands.

(a) Objectives of the sale of public lands: Taiwan had 180,000 chia of public cultivated lands. Before the sale, 59% was under tenant operation while most of the remaining 41% was operated by government corporations and agencies. However, low rental rates and secure tenure caused many peasants to compete for the lands and lands were often subleased at high charges. To wipe out such illicit practices, the sale of public lands was decided upon by the Government.

(b) The sales program was conducted as follows: All farmers tilling public tenanted lands were qualified to purchase them, but first priority of purchase was given to those tenants who had duly signed lease contracts with the Government. Qualified farmers could purchase all lands leased to and tilled by them without any restriction. Farmer purchasers paid the purchase price of 2.5 times an annual crop of the lands, according to the fertility, in twenty semi-annual installments spread over a period of 10 years. The payments were so adjusted that two semi-annual installments plus the annual land tax would not exceed 37.5% of the annual crop. The purchase price was paid in commodity; for the purchase of paddy field the payment was made in rice, and for dry land in sweet potato by converting it into cash according to the market value of sweet potato at the time of payment.

Land-to-the-Tiller Program

In 1952, the third measure to re-allocate private tenanted lands to tenant farmers, known as the Land-to-the-Tiller program went into action. This measure was carried out through the following steps:

(a) Purchase and resale of tenanted land by the Government: Under this program, each landlord, with certain exceptions, could retain a maximum area of three chia of medium-grade paddy field or its equivalent. Tenanted holdings exceeding that limit were purchased by the Government. Such lands were resold, along with immovable fixtures thereon, by the Government to the tenant farmers who had been tilling them.

(b) Compensation to the landlords: The Republic of China is different from other countries which have implemented similar programs in that it has developed two unique payment devices, namely, the commodity bonds and stocks of state enterprises to pay for the land purchased from

landlords. The bonds preserve the value of amortization payments against possible inflation They were issued in two kinds: the rice bond and the sweet potato bond. The rice bond was expressed in rice and was used to pay for the purchase of paddy field. The sweet potato bond was expressed in sweet potato and was used to pay for the purchase of dry land. Both kinds of bonds were redeemable in 20 semi-annual installments in 10 years at an interest rate of 4% per annum payable in kind. The stocks of state enterprises were used to divert a part of the private capital tied up in land to the field of private industry by transferring some of the state enterprises to private ownership. Four state enterprises, namely, the Agricultural and Forestry Development Corporation, the Industrial and Mining Corporation, the Cement Corporation and the Paper and Pulp Corporation, were sold by the Government to landlords to cover 30% of the total purchase price. Under the program, 1,272,109 metric tons of rice and 433, 262 metric tons of sweet potato were paid to the landlords for the land purchased by the Government. Of these two amounts, 70% was paid in commodity bonds and 30% in stocks of state enterprises in September 1953.

(c) Amortization of purchase price by farmers: The amortization of the land purchase price by farmers in the form of 1,525,211 metric tons of rice and 519,358 metric tons of sweet potatoes was begun in 1953. Each year, one-tenth of the above two amounts was paid to the Government in two installments including interest. Payment received each year amounted to 98% of the total amount due. Up to June 1962, 18 out of the total of 20 installments had been paid off by the 194,000 farmer-purchasers. The last installment was due in January 1963.

Results of the Rural Land Reform

The results of the rural land reform program to date can be shown by the following comparisons of 1949 and 1960 figures:

(a) Farmer families owning all or part of their land increased from 61% to 85% of the total.

(b) Owner-operated land in the whole island increased from 59% to 86%.

Land reform has produced important social-economic effects. The living conditions of farmers have improved, the rural economy and social order have become stable and progressive.

(a) Land reform gave a great stimulus to the productive incentive of farmers which, in its turn, has helped increase production on the farm. In 1949, the agricultural production index was 74 and in 1960 it increased to 131. The brown rice production in 1961 was increased by 68% as compared with that of 1949.

(b) After land reform, the net gains of a new owner-farmer from two rice crops harvested on one hectare of paddy field in 1960 increased by 155% as compared with his gains in 1948 when he was a tenant.

(c) During the period between 1949 and 1958, 225,000 new rooms were built and 662,000 rooms were repaired, 161,000 bicycles and 64,000 sewing machines were bought and 250,000 electric lights were installed among the more than 300,000 families of new owner-farmers who had emerged as a result of the land reform.

(d) Farmers can keep enough rice to feed their families and they frequently have more pork, fish or fowl to go with the rice. Many have new clothing every year and the children are better dressed. Over 96% of the school age children are going to school.

Future Plans

Although the land reform has improved the economic and social conditions in Taiwan as above, the Chinese Government is tackling the following problems to uphold the effects of the reform:

(a) Purchase of retained tenant holdings: After the completion of the Land-to-the-Tiller program, Taiwan still had 77,000 hectares of private tenanted lands retained in the hands of landlords, and 130,000 farm families working thereon as tenants and part-tenants, though some 61,400 families have already acquired a part of their leased holdings under the Land-to-the-Tiller program. To realize further the Land-to-the-Tiller ideal, the Chinese Government is undertaking a land purchase loan program under which the Land Bank of Taiwan is authorized to grant loans to tenant farmers to purchase the land they leased with a special fund set aside by the Government. The loan is for a period of 10 years and the maximum amount of any loan is 60% of the value of the land to be purchased with an interest of 5% per annum.

(b) Improving land use by consolidation of fragmented farm holdings: The farmers of Taiwan have been cultivating small areas of land consisting of many small plots which are widely scattered. Such a situation makes it difficult for the farmers to adopt modern methods of cultivation. Land reform has not changed this situation. To achieve the more rational use of land and to increase farming efficiency, consolidation of the fragmented land plots is now under way with government assistance. The Chinese Government plans to consolidate 300,000 hectares during the next 10 years. So far 10,000 hectares have been consolidated.

(c) Promoting savings and capital formation: Most of the tenant farmers who received land under the land reform program will have paid up their final installment of the land purchase price this year. In the best interest of Taiwan's economic development, it would be far better if the savings potential of the new owner-farmers could be mobilized at least in part for investment in farm improvements. The Government is conducting an educational campaign to assist farmers in planning their family spending and consumption.

SOME LESSONS FROM COLOMBIA'S EXPERIENCE WITH LAND REFORM

Albert O. Hirschman

[From Land Reform and Social Change in Colombia, Discussion Paper 4; Madison, Wisconsin, Land Tenure Center, The University of Wisconsin, November 1963.]

[The University of Wisconsin has for many years conducted research on the economic, social and political aspects of land tenure problems. In 1962, it established the Land Tenure Center in connection with a research and training contract between the University and the Office of Research and Analysis of the U.S. Agency for International Development. In its research, the Center has devoted particular attention to agrarian reform problems in Latin America. It has conducted nearly 70 seminars and workshops which have been attended by participants from developing countries and the United States. It publishes a monthly "Newsletter" and discussion papers and other materials on land tenure and agrarian reform. The publication from which these excerpts were taken reports the presentations and discussions at an all-day faculty seminar held in April, 1963. For additional information on the Center and its activities, write to: Professor Raymond J. Penn, Land Tenure Center, 310 King Hall, University of Wisconsin, Madison, Wisconsin.]

These are excerpts from the paper.

In my recent book [Journeys Toward Progress: Studies of Economic Policy-Making in Latin America, Twentieth Century Fund, 1963] on which the following remarks are

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based, I waged a sort of war on two fronts. One is a war against the naive view that you can have land reform, regional progress or control of inflation simply by sending an expert to convince the Minister of Finance that a change in policy makes sense; the view that a liberal political party winning at the polls with a 51% edge can straightaway accomplish land reform plus other good works, and all with no disturbances, no tensions. For example, some people in the Alliance for Progress now think that we can at one and the same time have a thoroughgoing land reform and an excellent climate for private investment, seemingly unaware that steps toward one objective make the other harder to achieve, at least in the short run.

My war on the second front is against the tough view of the typical Latin American radical, who believes that in order to achieve <u>any</u> change, you must change everything, that revolution is the absolute precondition for any progress. In my Brazilian chapter, I quoted a taxi driver, who, when we were stalled interminably in the famous post-office-hour traffic jam in downtown Rio, sighed, "We need a Fidel Castro here!" Ah yes, traffic will flow only through revolution. You cannot have economic development in the real sense, so this group argues, even though factories are going up; it's all artificial without land reform; and you cannot get land reform until <u>after</u> the revolution.

Now, frequently, we find that people swing suddenly from the naive view that all you need is to bring men of good will together to the tough view that insists on total revolution; especially among technical assistance experts, I have known quite a few who start out with the naive view and, after absorbing a certain amount of frustration, switch violently over to the tough view.

My aim is to alert people not only to obstacles but also to possible by-ways, to permissible detours toward progress even when the classical route seems to be obstructed. In pursuing that aim, it interests me always to note how certain weaknesses in a political structure or a cultural process can unexpectedly become elements of strength. The traditional economic development literature tends to talk about favorable and deterring factors as though these were two distinct natural elements that could never alter. However, historians have frequently noted that a factor that contributes at one time to a civilization's or a nation's strength turns into a source of weakness later on. I think the reverse can also be true, and that if we study how a country moves out of stagnation to progress, we will sometimes perceive that a so-called factor of weakness becomes -- with changing conditions -- an element of strength. Let us note as an example the very naiveté of the reformer. Like a chess player who hasn't been told that he is losing and might as well give up immediately, the naive reformer goes on stubbornly making move after move and occasionally, in the course of countless tries, he wins. In the process, he becomes a more wily maneuverer and picks up more allies than the pure revolutionary who stakes the game on a single gambit.

The hypothesis I started with -- that Colombian history might have some lessons to teach along this line -- has become stronger with detailed acquaintance, and I would like to indicate briefly a few of the features that seem to fit my theory.

Types of Land Holdings

When we look at the Colombian land tenure situation, the first thing to notice is the variety of patterns it includes. We have, of course, the traditional *hacienda* in many areas -- the Atlantic Coast, parts of the Cauca Valley, the Savannah -- large estates given over chiefly to cattle grazing, where *peones* till small pieces of land on the outskirts of the *hacienda* in return for furnishing their labor to the *hacienda*. It is true that the traditional semi-feudal pattern, *latifundio cum minifundio*, is still an important one although it has been restricted by various developments.

Also traditionally through a long history, there are small properties held by newly arrived settlers from Spain. Even in the early 1800's, the pattern of small-scale agriculture by enterprising immigrants was important, and it had a tremendous push in the second half of the century in the famous Antioqueño colonization that started out from Medellín to cover eventually not only the central slopes but also the inner slopes of both the west and east *cordilleras*. Today we have continuing trends of spontaneous colonization, people crossing the ranges over into the Amazonas basin and toward the Atlántico now that difficulties of climate and malaria are being overcome.

And finally, as a third pattern, there is the plantation. The plantation is of two different types: one, the permanent plantations such as those of bananas in the north and sugar cane in the Cauca Valley, and two, the very important new type of commercial cropping which changes from year to year in accordance with market demands and which impinges more and more on the *hacienda*. Operators of this new type of plantation are frequently people from the city who want to make a fast *peso* on a speculative basis and who discover that they can, with irrigation, do quite well in cotton, rice and barley. This new practice has made a very noticeable contribution to the total agricultural output in recent years and has led some observers to conclude, somewhat prematurely I think, that there are no longer any semi-feudal patterns in Colombia, that the land problems are in the process of being solved in this particular capitalistic fashion.

Periods of Agrarian Change

Actually, we must note that there have been a number of different steps in the transition from the orthodox system. The Antioqueño movement -- which took place at the time of increasing monopolization of

land in Porfirio Díaz' Mexico -- led to the breaking up of many large tracts that were nominally owned by single landlords. As people moved into the region, the owners were content to get a bit of monetary value out of renouncing a title here and there, and the haphazard transfers became established in the courts as a result of the actions of peasants and of the new municipalities that were built up during this migration period.

The second period of land break-up pivoted on the coffee plantations of the western slopes of the eastern cordillera. This area, from Bogotá down toward the Magdalena River, was one of large holdings. They were assigned by their absentee owners in Bogotá to coffee as an excellent cash crop and were worked on the traditional basis of peon labor in exchange for small subsistence plots. In the decade from 1927 to 1936, there was a breaking-up of land-owning patterns in this region, with a sharp increase in the number of fincas, while only gradual increases were occurring in other areas. Superficially, this change might be attributed wholly to the 1929 depression and the drop in coffee prices, but the truth is that a somewhat militant peasantry had started the movement toward change even before the coffee price broke. I have discovered a very interesting official publication of the period, which documents the back-and-forth maneuvering that preceded the famous Law 200 of 1936. This publication has eye-witness reports on the numerous claims and disputes between owners and peasants and the not always consistent intervention of state authorities; it provides a fascinating study of the skirmishes that occur before a law comes into being. Among the principal points of dispute was the peones' wish to grow their own coffee trees, which the landowners were trying to repress in knowledge that peones who owned the trees would cease to be truly peones.

A third critical step, which I have already mentioned, was the emergence since World War II of commercialized agriculture, the appearance on the scene of the capitalist entrepreneur who rents or buys 100 acres or more from a large owner. Some people have said that now we have an unholy alliance between the former feudal landowner and the new industrialist who is attracted by the prestige of landowning and wants to join the traditional society. This is very bad, these critics claim, for some of the capital that might be available for industrial development gets drained off. Perhaps this is true in some cases, but usually we find that when the city man moves onto the land, he can't help being himself. He is less apt to be infected by the lazy old absentee owner's spirit than to infuse his own spirit into agriculture. We certainly have some evidence that when people who have made their money in trade or industry turn to land investment -- even though tax saving and prestige hunting may be part of the motive -- they get real satisfaction out of showing the old landlords a trick or two and of opening new frontiers for their skills in management.

Factors Working for Change

So, in spite of the seeming rigidity of Colombia's situation, I feel that there is much room for maneuver and that all kinds of strange things can happen. One of the strange things that did happen takes us back to that period during the late twenties and early thirties when a very considerable amount of land was taken up by the squatters. The break-up was a result, not of an agrarian revolution, but simply of a decentralized kind of initiative on the part of the peasants, a decentralized violence that was eventually legalized by the state in Law 200. Indeed I believe that Law 200 is one of the big accomplishments that is often ignored. It is much criticized in Colombia, and in most of the literature on the subject, as having been completely ineffective, because of Article VI, its one poetic article (which every law must have) that looks toward the future and seems hardly meant to be taken seriously. Article VI says that in ten years' time when certain lands are found not to have been properly utilized, they will revert to the state. Well, this was a strange declaration, for if you want revolution and great changes in agrarian tenure, you cannot legislate them for ten years hence. It was clear to anyone that this was a programmatic portion of the law such as the clause in the Brazilian constitution of 1891 saying that a capital is some day to be built in the center of the country. (Well, eventually -- 70 years later -- Brasilia was built.)

But the real accomplishment of Law 200 was in Article I, which legalized the status quo, the _situaciones de hecho_. This meant that all these silent decentralized actions of the peasants were given sanction -- every one acquired title to the plot of which he had taken possession. In the existing society still dominated by its old institutions and old power structure, it would have been quite impossible to achieve this feat by the theoretically normal or orthodox sequence. According to our radical reformers we would first have needed a revolution and then we could legislate the break-up of the _hacienda_. But instead, Colombia invented a disorderly sequence where first the _hacienda_ is broken up and then this situation is legalized. And this could be done within the existing society.

What other ways are there of breaking up a solid front and of introducing changes by indirection in Colombia? I have already hinted that the landowners are no longer a homogeneous group. There is a definite split today between the old types who are content with getting some income from the land as a way of life and the progressive new landowners who are interested in economic use and maximum income from the land. This split has been particularly sharp in the Cauca Valley where the regional planning agency, CVC (Cauca Valley Corporation), has been supported by the progressive group of industrialists, landowners and cane growers and has been stubbornly opposed by the _Asociación de Ganaderos_ who held to the ancient belief that there were only three good businesses

in the valley: cattle ranching with good administration, cattle ranching with bad administration, or cattle ranching without administration. Growing out of this cleavage, we actually got some support during the fifties from these progressive landowners for land-tax measures that would thereby induce their brethern, so to speak, to utilize their land better or else to rent or sell it to those who would exploit it efficiently. Certainly it would be difficult to enlist these capitalistic new owners for measures of land reform per se, but their critical view of their inefficient colleagues won their support for certain tax measures.

Balance-of-payment pressures also played a useful role in drawing attention to land uses and brought some unexpected alliances in Colombia when the coffee price broke and there was need to have a good look at the source of trouble. The first thing that Colombians saw to their great amazement was that they were importing 100 million dollars' worth of foodstuffs. "What's wrong with us," they ask, "that we're importing oil seeds, cocoa, wheat, barley, cotton, etc.?" Public discussion of the need for better methods of farming enlists the central bankers and finance minister to press for results in that sector of the economy. It also leads to experiments, not directed to land reform, but to new proposals, tinkering with tax matters, and so on. These in turn may make people ready later on for land reform if the tax measures prove ineffective or unenforceable.

Another interesting lesson we can draw from Colombia's policy-making experience is that old and accumulated legislation which seemed to mean nothing can come in handy at a later date. Unsuccessful poetic legislation leaves traces on the statute books, and one day when public opinion and political power are such that the country is ready to do certain things, its administrators can look through the books and find that they have practically all the authority they want.

Here is one striking example of how an ambitious, unenforced and utopian law proved helpful at a critical moment. The 1936 Constitution, put through during the heyday of the Alfonso López regime, a Colombia New Deal period _par excellence_, contained an article concerning expropriation. The first sentence says that property can be expropriated against compensation in cash. That is, of course, a feature of almost all Latin American constitutions and a stumbling block today in terms of land reform for governments which would like to pay in bonds and avoid the inflationary consequences of cash payments. But the following sentence in the Colombia Constitution -- which perhaps no one noted at the time -- is unique in Latin American constitutions: it states that you may also expropriate without _any_ compensation, if such expropriation is required on grounds of equity and if both houses of congress vote in favor of it. This little clause _was_ noted by Carlos Lleras Restrepo, who authored, shepherded and engineered the many compromises on the land reform bill that was passed in 1961. When the

question of compensation in bonds came up and people argued that it was unconstitutional, he said, "Not at all. The 1936 Constitution gives us the right to expropriate even without any compensation. Quién puede lo más, puedo lo menos -- one who can do the maximum can also do the minimum, and hence we don't need any new constitutional provision to enable this law." His reasoning was accepted and permitted a statute that is quite generous in terms of payment, but in any event represents a feasible provision for compensation.

Still another way in which a long experience of unenforced legislation sometimes proves helpful to a cause like land reform is that legislators continue to pass laws in the comfortable belief that their laws won't amount to anything. "It's just another law...it will get us votes and the leader asked for it...we'll have to play along but we'll be able to block it later on." Then occasionally one of these seemingly playful laws will work, to the surprise and dismay of the people who passed it.

Land Taxation and Land Reform

This habit of not taking general legislation too seriously may explain why drastic land reform laws tend to pass more easily than mild taxation laws. Taxation applies across the board -- you expect it to hit you -- whereas land reform sets up a selective mechanism that will expropriate here and there on a case-to-case basis, so that the individual landowner trusts the measure may never affect his particular property and his own pocketbook.

Certainly it has proved immensely difficult to carry through effective land taxation in Colombia, though there is at last some tinkering with tax measures. The idea of taxing land was already in the air during Alfonso López' time, but it took no shape. Then during the survey of the International Bank for Reconstruction and Development in 1949-50, there was wide public discussion that land should be taxed on some basis. However, the Bank mission was not able to convince the Colombian government of the merits of its proposed plan, perhaps because it was too complicated a scheme. Several later tax attempts were made both by the Rojas Pinilla regime and by the military junta, which actually put a law on the books that prescribed tax penalties for landowners who did not cultivate their land in adequate proportions. But, this decree met with collection problems at the hands of local power groups and demonstrated the well-known fact that taxation is extremely difficult to enforce when the existing power structure is not sympathetic to its aims.

This is a complicated subject and theorists differ on whether a government can extract more tax money out of large landholders or out of the peasant holders of small plots. I am inclined to agree with

Philip Raup [see pages 10-11] that it may prove easier to tax the peasant if he acquires with his land a true stake in it and a motivation for wanting the improvements, education and services that tax moneys can provide.

Indeed, it came home to me as I looked at the many rather fruitless efforts in Colombia that the great difficulty in pushing through tax measures is that nobody is in favor of taxation. Many are against it -- all its prospective victims -- but who actually profits from taxation? In Latin America there is a general idea, I think, that revenue is going to be squandered, and the prospective tax victims can always convince the public that their money will be put to much better use by them than by the government.

Revenue itself has no political appeal; you must have first a definite expenditure and you must rally political and social forces in favor of that expenditure so that people will believe that revenue is needed. After all, the big tax decisions in the developed countries have mostly been taken under the impact of wars and great economic national crises. And, in Colombia, the one notable instance of success with land taxation was CVC's ability to push through a territorial law that practically doubled the real estate tax with CVC as the immediate beneficiary. Here you had a venture in economic development that got off the ground and was able to rally the Cauca Valley people's support for its costs, even against very strong resistance from the landowners. It seems useless to preach tax reform to Latin America today unless it is linked to compelling and understandable reasons for increasing the tax bite. In fact, I've recently argued that inflation in Latin America serves a purpose in convincing people that you must tax to avoid depreciated currency.

Unjustified Defeatism in Latin America

My conclusion about the tax experience is, as I suggested earlier, rather unorthodox, because instead of saying land taxation has been a failure -- one more fracaso -- I would say it has been extremely useful in preparing the ground for land reform, just as it was the alleged failures of the Law of 1936 that convinced people they had to do some tinkering with taxation. This fracaso manía -- as one might call it -- so characteristic of the whole Latin American scene, is certainly strong in Colombia. The Colombians' own conviction that Law 200 was a failure infected the North American literature on the subject, but my belief is quite different, as I have tried to indicate. Similarly, people were so convinced that Decree 290, passed in 1958, was going to be a failure that they made sure it was never given a chance to be applied. Even so, this decree, with penalties and benefits for desired crops to cut down on imports, did have some good effects, for it added to the push in commercial plantations.

Now Law 135 of 1961 is already being given the same treatment. In my correspondence with Bogotá friends while it was being formulated in parliament, I heard, "It will never pass. It is hopeless with our kind of Congress." Then as soon as it was passed, I got the story, "Well, it won't amount to anything. It won't be enforced." But, there was the extraordinary experience of the first six months during which the Ministry of Agriculture and the newly created Institute [for administering the agrarian reform program] put through decrees which strengthened the law very considerably. The original law set no criterion for the value of the to-be-expropriated properties, but a decree now states that the value is not to exceed 130% of the cadastral value. That was an astonishing and very decisive step in making the reform less expensive and potentially much more far-reaching than it could have been if they had used as a basis the commercial prices of property.

Now my Colombian friends are probably saying, "We've been sitting around six months, and how many hectares have been distributed?" But, it was rather important to get these points clarified before the next administration came in and thereby at least put the onus on the new administration if it goes back on the decree that gives real teeth to the law.

Why do we have this attitude of _fracaso_? This insistence on counting everything that is being done a failure? To be true to myself, I must claim that it serves some function, that in some situations it can be an energizing attitude. If a man coming into power has the chance to say, "Nothing has been done. I will show you what _I_ can do," instead of feeling hemmed in by the records of his forefathers, then he can devaluate all that has gone before and, starting from zero, make anything he achieves seem so much to the good. It is about like taking over an asset that has been written down so completely that you can forget the initial cost.

We also find, interestingly enough, in Latin America, a completely different attitude: that is, when a problem merely begins to be solved, it is sometimes classed as wholly solved. There is a tendency to say, "Ah well, it is no longer interesting. Let's do something else that's more interesting." In either attitude, public policy is not conceived as a tool that supplements other efforts at resolving long-term situations, but more as a sovereign weapon of attack for each new policy maker.

THREE BOOKS ON AGRARIAN REFORM

United Nations, Department of Economic and Social Affairs, Progress in Land Reform; Third Report; New York, 1962, vi and 104 pp., United Nations Publication Sales No.: 63.IV.2, US$1.50.

This is the third progress report on land reform prepared jointly by the secretariats of the United Nations, the Food and Agriculture Organization, and the International Labor Organization. The previous reports were issued in 1954 and 1956. In addition to summarizing progress in land reform by region and by country, the third report also contains chapters on the relationships between land reform, on the one hand, and agricultural productivity, output, employment, wages, and living conditions, on the other hand; on the financing of land reform; and on land reform and community development.

U.S. Department of Agriculture, Economic Research Service, Farm Economics Division, Agrarian Reform and Economic Growth in Developing Countries; Washington, D.C., March 1962, 74 pp., free.

This publication contains papers by well-known U.S. experts prepared for a seminar on research on agrarian reform and economic growth in less developed countries. Subjects covered include the role of research in agrarian reform; agrarian reform and economic growth; characteristics of and improvements in agrarian reform programs; and the legal and economic aspects of agrarian reform. The seminar was sponsored by the North Central Land Tenure Research Committee, the Farm Foundation, and the Farm Economics Division, Economic Research Service, U.S. Department of Agriculture.

Froehlich, Walter, editor, Land Tenure, Industrialization and Social Stability: Experience and Prospects in Asia; Milwaukee 3, Wisconsin, the Marquette University Press, 1961, xv and 301 pp., US$9.00.

Held under the auspices of Marquette University with the financial support of the Asia Foundation, a 1959 conference at the University brought together leading Asian and Western experts for discussions on land tenure and its relationships to economic, political and cultural change in individual Asian countries, including Mainland China. The papers and proceedings of the conference are published in this volume. They cover both empirical and theoretical aspects of the relationships under study and, together, make a major contribution to the understanding of these complex interrelationships.

THE UNITED NATIONS CONFERENCE ON TRADE AND DEVELOPMENT

RESEARCH BEFORE AND AFTER THE UNITED NATIONS CONFERENCE ON TRADE AND DEVELOPMENT

The United Nations Conference on Trade and Development (UNCTAD) was held in Geneva from March 23 to June 16, 1964. The Conference was concerned with several major subject areas in the general field of the relationships between the trade of the less developed countries and their development. These were: removing obstacles to the expansion of the trade of the less developed countries; devising guidelines for appropriate international commodity arrangements affecting their primary product exports; expanding their export of manufactures and semi-manufactures; facilitating the financing and marketing of their exports and imports; improving their earnings from and reducing their expenditures for nonmerchandise transactions; and establishing continuing institutional arrangements within the framework of the United Nations for dealing with the trade problems of the less developed countries. The Conference concerned itself mainly with the policy changes and action programs which the developed countries, both Western and Communist, could undertake to help expand the trade of the less developed countries.

A considerable number of studies were prepared during the 18 months prior to the Conference in the foregoing subject areas. The Secretary General of the Conference, Dr. Raúl Prebisch, wrote a comprehensive report, <u>Towards a New Trade Policy for Development</u> (United Nations, New York, 1964, Sales No. 64. II. B. 4, US$1.50), which drew upon other studies and reports undertaken by international agencies and the United Nations Secretariat during the pre-Conference period and upon the deliberations of the Conference's Preparatory Committee. In addition, many

studies and reports were also prepared by participating countries and by individual experts. It was hoped that, together, all of the reports would constitute a working basis for the Conference.

In addition to the basic statistics on world trade and production, the pre-Conference studies and reports included various estimates of future growth possibilities and trade needs of the less developed countries; analyses of problems relating to primary product exports and international commodity agreements; surveys of the problems and possibilities for the export of manufactured and semi-manufactured products by the less developed countries; analyses of problems relating to the invisible (nonmerchandise) items in their international transactions; possibilities for increasing the financing of the trade of the less developed countries; special country and regional trade problems; the implications for the trade of the less developed countries of regional groupings among both developed and developing countries; and possible new international organizational arrangements in the trade field. The studies and reports prepared prior to the Conference are listed in United Nations Conference on Trade and Development Document E/Conf. 46/1, March 4, 1964.

The Final Act of the Conference, containing its resolutions and recommendations, specified numerous studies to be undertaken during the post-Conference period by various UN agencies, by special intergovernmental working groups, and by the new UN agency to be established to carry on the work of the Conference. However, by no means all of the studies mentioned in the Final Act require research and analysis by experts; the term "study" is also used to refer to intergovernmental discussions and negotiations leading to agreements regarding subjects on which new research is not likely to be required.

Among the recommendations for research studies to be undertaken in the post-Conference period are:

1. The continuing trade organization should collect and analyze data not now available with respect to primary products which less developed countries wish to include in commodity agreements.

2. The UN Secretary General should arrange with the International Bank for Reconstruction and Development (IBRD), the UN regional commissions and other appropriate regional bodies for a study of the problems of regional development.

3. The IBRD should expedite its study of the possibility of establishing a system of investment insurance for direct private foreign investment in less developed countries.

4. The IBRD should study the problem of guarantees for the securities of private and public enterprises of the developing countries which are floated in the capital markets of the developed countries.

5. The continuing trade organization should undertake a study of the export marketing systems for the main primary products in order to determine the factors affecting the shares of the final price which accrue to exporting and importing countries.

6. The IBRD should study the use and terms of suppliers' credits and credit insurance, including rediscount arrangements, for financing exports from the developed to the developing countries, with respect particularly to the latter's capacity to repay and to the effects on international competition.

7. The IBRD should study the possibilities for providing supplementary financing on a long-term basis for shortfalls in export proceeds which disrupt the development efforts of the less developed countries and which would be available to the latter after they had exhausted the short-term compensatory financing provided by the International Monetary Fund.

8. The Secretary General of the Conference should convene a group of experts to study international monetary issues relating to trade and development with special reference to the objectives and actions of the Conference.

9. The IBRD, International Development Association (IDA), International Finance Corporation (IFC), UN Special Fund, and other appropriate intergovernmental and nongovernmental agencies should undertake, in their respective fields of competence, studies and research on the expansion of tourism in the less developed countries on both a national and regional basis.

10. Appropriate UN agencies and the continuing trade organization should survey and analyze the economic and social problems of depressed areas within the less developed countries.

11. The competent international bodies -- including, if appropriate, the continuing trade organization -- should study the economic situations, policies and plans of developing countries to determine the feasibility of attaining higher rates of growth (a) than those experienced by most developing countries during the past ten years and (b) than envisaged for the UN Decade of Development, and to analyze the measures which would have to be taken by both developing and developed countries to achieve such higher rates.

It is anticipated that many, and possibly all, of the pre- and post-Conference studies will eventually be published either by the UN or by the other international agencies undertaking them. Also, the UN expects to publish by the end of the year the proceedings of the Conference, containing the Final Act, addresses to the Conference, the reports of the main Committees, summaries of the Conference discussions, and a list of all the studies and other documents prepared for the Conference. When published, this will be designated as Conference Document E/Conf. 46/139.

FINANCIAL AND FISCAL POLICIES IN DEVELOPMENT STRATEGY

Development policies and activities of governments which do not directly involve capital investment have in recent years been assuming increasing importance. Not only do they affect the rate and character of economic growth but they also are capable of mitigating or increasing the constraints imposed by other factors upon a country's development. The papers presented in this section deal with certain aspects of non-investment policies which are of particular significance. These are: the capacity of developing countries to service external debt obligations and the implications for their development prospects; the relationships between the balance of payments and different types of development strategy; and the effects of different kinds of taxes in stimulating or inhibiting development.

THE EXTERNAL DEBT SERVICING CAPACITIES
OF DEVELOPING COUNTRIES AND THE
IMPLICATIONS FOR DEVELOPMENT POLICIES

Dragoslav Avramovic

[From Economic Growth and External Debt, Volume I, An Analytical Framework; Staff Study of the Economic Department, International Bank for Reconstruction and Development, Washington, D. C., 1964, mimeograph, pp. 63-70.]

[This study was prepared at the request of the Development Assistance Committee of the Organization for Economic Cooperation and Development and of the Secretary-General of the United Nations Conference on Trade and Development. It consists of three parts. Volume I sets forth a system of analysis of the debt servicing burden of the developing countries, its changes over time, and the relationships of debt and debt service to major economic variables -- rate of income growth, rate of investment, rate of return on capital, rate of export growth, fluctuations in external accounts, and balance-of-payments policies. The analysis covers separately the liquidity and the long-term growth aspects of debt servicing problems. Volume II contains the statistical data and quantitative analysis required for the study. Volume III consists of technical monographs dealing with various aspects of export fluctuations and debt servicing problems; long-run growth and debt servicing problems; and with the further research needed in order to clarify the policy issues.

Excerpts from the study begin on the next page.

Dragoslav Avramovic is Assistant Director, in charge of the Economic Department of the International Bank for Reconstruction and Development. He was assisted in the preparation of this study by staff members of the Economic Department.

Volumes II and III were prepared by the staff of the Economic Department of the IBRD under the direction of Dragoslav Avramovic. The analyses and conclusions represent the views of the authors and not necessarily of the IBRD or of the organizations at whose request the study was undertaken. The three volumes will be published by the Johns Hopkins Press, Baltimore.

The excerpts presented here comprise most of the concluding chapter of Volume I.]

Any borrowing on conventional terms results in a return flow of interest and amortization in fairly rapid succession. In the case of foreign borrowing, debt service payments are a charge on domestic real income and savings. These payments have to be transferred abroad either by expanding exports, by curtailing imports, or by further borrowing abroad. Capital inflows and, particularly, exports of primary producing countries are fluctuating. In contrast, debt service on public and private loans is contractually fixed.

Inflexible obligations are potentially dangerous under any circumstances. This danger was present even in the classical system of foreign investment in earlier centuries of economic and financial history. The unmitigated violence of the international business cycle, at that time, frequently created havoc in international investment. There were, however, two redeeming features. Foreign private direct investment probably accounted then for a major share of total flow, and it was concentrated largely in activities producing primary products for export; and as export sales fluctuated, so did profits in the export industries. The other redeeming feature was the complex inter-relationship of interest rates, risk premia and the anticipated behavior of debtors in periods of crisis. It was expected that borrowing governments would default occasionally on their fixed-term loans when a depression reduced exports and budgetary income or when budgetary policies were highly questionable. To offset this, debtors were charged an interest rate which included a risk premium high enough for the lenders to feel that chances of repayment were even or better than even. Probably the risk premium also included an insurance against wars and international inflations. Who was the winner in this game, played by creditors and debtors, we do not know. What is relevant for this study is the fact that a mechanism to cope with fluctuations did exist and in its own way, it helped to accomplish the major function of international investment: transfer of resources from countries with a plentiful supply of capital and correspondingly low rates of interest to countries needing capital and ready to pay higher rates of interest.

The present situation is different from that described above. A major part of private direct investment still flows to export industries

in less developed countries, although the products that are developed are new: instead of tea, cocoa and rubber plantations, foreign capital now finances aluminum smelters, iron ore mines, and above all, oil fields. The return flow of profits from these "enclave" investments fluctuates pari passu with export sales. But another part of foreign direct investment in the developing countries now goes into industries that produce goods to replace imports, be it fertilizer or steel. The profit rate in these industries is high enough to offset the heavy risks accompanying foreign investment and still yield a surplus above what can be earned in the major financial centers of the world. Sales of these goods on the domestic market in developing countries are rising rapidly and steadily. Since fluctuations in sales are minor, profits also tend to show an uninterrupted upward trend. A large part of profits is reinvested in productive assets and therefore serves to expand further the productive base of the economy. But the share of profits that is not reinvested becomes a charge which does not vary in response to export fluctuations.

Most developing countries now consider the acceleration of economic growth a major task facing the present generation. Growth targets are ambitious compared to resources that can be mobilized domestically for financing investment needed to achieve these targets. The responsibilities of governments in promoting more investment and faster growth are probably greater today than they were, on the average, in earlier periods of economic history. Therefore, there is demand for massive capital inflow from abroad, and the major channels through which this inflow is transferred are governments in developing countries, which either borrow on their own account or guarantee loans made to private parties. To the extent that this capital inflow occurs on "hard" terms, a rigid claim is built into their economic systems, consisting of contractually fixed debt service obligations. And as capital inflow proceeds, these contractually fixed obligations also increase. True, the debtors are in a much better position today than in earlier periods, because they are now charged less than 6 per cent for "hard" money and even less for some other forms of capital transfers. The lenders, or more accurately, their governments, have assumed the risk of default. A new concept of international financial morality has developed. Debtors should not default, precisely because they are charged moderate rates of interest and sometimes no interest at all. Nevertheless, the debt service charges do increase over time, since capital flows are expanding.

The percentage share of export earnings absorbed by debt service will rise under any circumstances. However, if world demand for primary products rises only moderately; if possibilities to expand exports of light manufactures are circumscribed by restrictions resulting from concern with domestic employment in the importing countries; and if it takes time to develop competitive exports of heavy industrial goods, it is virtually inevitable that the ratio of debt service to export earnings

will increase quickly and will attain a high level. This rigidity of the balance of payments will be further aggravated by a likely shift in the composition of imports of the developing country, as purchases of raw materials, fuels, spare parts, and sometimes even basic foodstuffs, rise rapidly. In short, if the return of capital, borrowed and domestic, is maximized by concentrating on activities catering to the domestic market, economic growth and structural change of the economy will be accompanied by increased rigidity in external accounts.

We do not know how long it takes a developing country to overcome the worst phase of the strains on its balance of payments. In particular, we do not know at what speed an industry which has been built initially to supply domestic needs, can be made sufficiently competitive to penetrate the international market. There are industrialized countries which have accomplished the transition from domestic to export orientation swiftly, in about a decade or so. It is impossible to say how representative or accidental their experience is. Sooner or later, if economic growth is a success, the structural change of the economy will inevitably lead to a structural change in external accounts, with a consequent rapid rise in exports and the relaxation of rigidities. But in the meantime and for the foreseeable future, debt service as a proportion of export earnings will be very high and the sensitivity of the economy to declines in its capacity to import will be very great. Under these conditions, even minor fluctuations in exports and minor policy errors of the borrower may have major repercussions.

The problems of rigidities and fluctuations and of financial danger that they imply, are only one aspect of the debt servicing capacity of the developing countries. From the long-run point of view, there are three other factors that are of fundamental importance:

> First, the rate of return on projects must be higher than the international rate of interest. Otherwise, no basis exists for successful servicing of foreign capital on conventional terms.
>
> Second, the savings out of newly generated income must be sufficient to enable the economy to finance an increasing proportion of its own investment requirements out of domestic resources. At some point in time, aggregate domestic savings must exceed aggregate domestic investment by a margin that is sufficiently large to meet at least interest charges on the previously incurred debt. If that point is never reached, funds would have to be continuously borrowed and indebtedness would have to increase continuously just to meet interest; and as new borrowings would also carry interest, the debtor would be caught in the familiar trap of the compound interest law.
>
> Third, the total flow of investment projects in the economy must be sufficient to yield an increase in aggregate national output

at a rate in excess of population growth. Otherwise, it may be presumed that popular pressures would interfere with debt servicing; and also, the flow of domestic savings is unlikely to expand sufficiently unless aggregate real income rises reasonably fast.

The developed countries have three choices in financing the economic growth of the developing countries. First, they may decide that in some countries day-to-day financial dangers are so serious and the long-term prospects for growth so uncertain that the only safe way out is to provide most of the needed funds on "soft" terms. This device is, of course, already being employed on a large scale (including the disposition of surplus foodstuffs on concessionary terms), although there is some tendency for countries that have made extensive use of this device to harden their terms, partly because other leading capital-exporting countries have continued to provide development assistance wholly or predominantly on a "hard" basis. If "soft" funds cannot be mobilized adequately, and if it is thought that it would be risky to expand "hard" lending, the second choice is to put arbitrary ceilings on the flow of funds that are made available to countries where the situation looks precarious. Depending on where the ceilings are fixed, the consequence may be that a number of profitable projects would not be undertaken because of the lack of finance, and the actual rate of economic growth in such developing countries may fall short of the technically and economically feasible rate. The third choice is to try to live with the dangers and with the risks and to finance growth predominantly at "hard" terms.

In practice, of course, all three alternatives are present. The mixture has varied and will continue to vary, depending on the judgment of the circumstances of particular countries and on the actual availability of "soft" funds. For analytical purposes, however, it might be useful to state, in somewhat more formal terms, the conditions which would have to be met for the mechanism of international lending at "hard" terms to work reasonably successfully. The assumption is that no arbitrary ceilings on lending are set and that all projects whose yield exceeds, with a reasonable margin, the international rate of interest (say, 6%) are financed.

The conditions are as follows:

(i) The creditors agree to lend continuously despite high debt service ratios (very high in some countries) and despite the general rigidities in the balance of payments of their debtors. The length of the period of lending depends on how far particular debtors are from the point of "self-sustained" growth. Self-sustained growth is defined to mean a rate of income increase of, say, 5% per annum financed out of domestically generated funds and out of foreign capital which flows into the country because it wants to do so. The only point which

may be added is that, as time goes on, gross capital exports would have to become very large if they are to yield a net addition to resources of the borrowing country. Such net addition takes place only when gross borrowing is in excess of repayments and in excess of interest due on the debt already outstanding. Since new borrowing also carries interest, the outstanding debt is compounded and this in turn increases the debt service that is due. The practical implication is that, in many countries, the mechanism of "hard" lending could not work properly unless at some point a substantial part of foreign borrowing were put on a non-project basis.

(ii) Difficulties in servicing debts have always been experienced, and they will continue to be experienced, whether we deal with debts of individuals, corporations or governments, and whether debts are domestic or international. The problem which concerns us here is how such difficulties can be reduced to a minimum. The massive transfer of resources from the rich to the poor countries -- which will have to last decades and which is needed to enable the developing countries to create the basis for self-sustained growth -- could not be undertaken on a "hard" loan basis unless the paramount condition of any loan is respected: loans have to be serviced, no matter what. Moreover, all other bills -- for imports, services, etc. -- must be paid on time as well. Only if this is done, can the bankers in good conscience mobilize capital from savers in the rich countries and send it to distant lands. Only then can they look with leniency at the rigidities in the balance-of-payments structures of their debtors and at the risks that these rigidities entail. Unless confidence is created that bills do get paid on time, the lenders would have to charge a rate of interest which would incorporate a premium to cover the risks. Such an interest rate might be much higher than the majority of debtors would be able to afford. Even more likely, the required flow of capital would simply not take place.

The task of managing the balance of payments in a developing country is formidable. It is so because effective demand within the country is great -- investment activity is high and accelerating. This does not mean that maintaining a desirable rate of economic growth necessarily conflicts with balance-of-payments equilibrium. Cases still exist where the propulsive force in economic growth is expansion of exports and where conservative fiscal and monetary policies are the best policies to pursue. Politically courageous policies can extract through taxation resources needed for development, and it is also possible, to resist the temptation to finance fixed investment with short-term credit. Where these circumstances do not prevail -- and this applies to a large number of the developing countries -- it will be necessary to attempt to insulate the balance of payments from domestic inflationary pressures. In any case, the limits within which governments of the developing countries, which are heavily indebted abroad, can act have become very narrow and the tolerances very fine. If

creditors are asked to live with liquidity dangers, the debtors should be asked to exercise restraint and act courageously.

(iii) Neither lenders nor borrowers will be fully able to handle the liquidity problems unless export earnings of the developing countries attain some measure of stability. It is true that the international business cycle today is something quite different than it used to be. Violent downswings in prices and quantities, so typical of earlier international financial history, have been absent in the two decades since the end of the war, and there is no present indication that they will recur. Occasional downward fluctuations in export earnings of the less developed countries, however, still occur. Much advance has been made in mitigating the impact of these fluctuations, both by the actions of the International Monetary Fund and by public lending agencies of the industrialized countries. But it is generally agreed that the problem is still with us and that much remains to be done.

(iv) Even if conditions (i), (ii) and (iii) are met, the process of "hard" lending cannot be expected on a large scale in countries whose existing debt structure is extremely unfavorable until some solution to their liquidity problem is found. In several countries, which are large international debtors, pending payments are extremely high. No solution of their present liquidity problem is likely to prove lasting, however, unless advance is made in coping with the root causes of the present difficulties. And it may be that developmental returns to capital in some of these "cash-squeeze" countries are high despite inadequate financial policies; but these investment opportunities cannot be exploited unless the liquidity crisis is resolved.

(v) From the long-run point of view, the developmental returns are decisive. If there are countries in which these returns, properly estimated to include both the direct and indirect benefits, are below the international rate of interest, it does not make sense to transfer capital to these countries on conventional terms. We do not know whether such cases exist, but it is quite possible that among the 100 countries currently engaged in the developmental process there are some where natural obstacles and lack of skills are such as to keep the rate of return below the rate of interest, at least for some time to come. If it is considered that these countries ought to be helped to develop, it would seem that lending to them on "soft" terms is the only solution.

(vi) It is not sufficient, however, that the rate of return on individual projects be in excess of the international rate of interest to justify lending at "hard" terms. The plough-back out of increased income must be sufficiently high to make it possible for the country to reach a stage in which it can pay out of its own resources for all

the investment that is needed to attain a satisfactory rate of growth. This condition -- the marginal savings rate sufficiently above the average savings rate -- can be met only if fiscal and monetary policy is conducive to generation of public savings and if private entrepreneurs are optimistic enough to plough back a large proportion of their profits into domestic activities rather than in investing abroad. The achievement of a sufficiently high savings rate is the sole responsibility of the borrowing country. Here creditors cannot provide much help. If they have a basis for judgment that domestic savings will not equal domestic investment requirements in the foreseeable future, however distant, lending on "hard" terms cannot do the job. Whether creditors, under these conditions, want to help the country by providing "soft" money is a decision which only they can make taking into account whatever objective obstacles stand in the way of progress of the borrowing country.

There are countries where the present level of income is very low, population extremely large and natural resources limited in relation to population. In these cases, return on particular investments may be high and the plough-back of profits generated by these investments may be large, and yet the aggregate rate of savings may remain low. If, despite being low, the aggregate rate of savings is increasing gradually, it is possible that ultimately domestic savings will exceed investment. The time span may, however, be extremely long and consequently, the gross capital inflow that will be needed, and the indebtedness which would result from financing the country predominantly on hard terms, may be extremely high. These are so-called "long-haul" countries. We hope that they are few, but they may be very important in relation to the total population of the developing countries.

(vii) For growth in income and in savings to materialize, there should be a sizeable number of investment projects started yearly. In other words, the aggregate investment rate must be at a sufficiently high level. Unless this is accomplished, the whole process may never "get off the ground," because population growth may continually be catching up with income growth. It is primarily the responsibility of the debtor country to develop profitable projects, but the industrialized countries can provide help which may prove decisive.

The successful growth-cum-debt process ultimately depends on four variables: the size of the investment activity which a developing country succeeds in undertaking, the rate of return on investment, the rate of plough-back of the increment in income generated by the new investment, and the international rate of interest charged on borrowed loan capital. It is a matter of policy which one of these variables will be chosen as a target of policy action. In some developing countries, it will suffice to raise the absorptive capacity and thus attain

a higher rate of investment consisting of high yielding projects. In all of them, it is necessary to attain a high rate of plough-back, and thus raise the average rate of savings which is the ultimate determinant of self-sustained and independent national economic growth. And for some of them, the international rate of interest -- that key variable in the process of growth-cum-debt -- will have to give if the international investment system is to function with tolerable smoothness.

Thus, the policy questions which are posed by this study are serious. They are whether full interest will be charged everywhere, how the present liquidity crises in several countries can be successfully overcome so that the growth process can be resumed; and, perhaps above all, how the absorptive capacity for high-yielding projects can be increased. It may be very difficult to find a solution to these issues, and, in any case, they probably require the concerted effort of both lenders and borrowers on a scale and in harmony which would be without precedent. But the task, itself, is also without precedent.

FISCAL POLICY AND THE BALANCE OF PAYMENTS OF DEVELOPING COUNTRIES

Harry G. Johnson

[From "Fiscal Policy and the Balance of Payments in a Growing Economy," a paper presented at the Third Study Conference on Problems of Economic Development: Government Finance and Economic Development, sponsored by the Organisation for Economic Cooperation and Development, and held in Athens, December 12-19, 1963.]

[The subject of the Conference for which this paper was prepared was government finance and economic development with particular reference to the problems of the less developed member countries of the OECD -- Greece, Iceland, Portugal, Spain, Turkey, and Yugoslavia. However, several of the papers presented, including the one excerpted here, deal more broadly with important aspects of monetary and fiscal policies in the less developed countries throughout the world. The papers of this Conference will be published in book form by the OECD in the autumn of 1964 under the title <u>Government Finance and Economic Development</u>. The papers of the first two OECD Study Conferences were published as <u>Regional Economic Planning: Techniques of Analysis</u> (1961) and <u>Methods of Industrial Development</u> (1962).]

This is a reprint of most of the paper.

From the analytical point of view, the availability of economic relationships with the rest of the world facilitates economic development in two major ways.

<u>First</u>, at the macro-economic level, the rest of the world furnishes a source of savings additional to

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what is forthcoming, or can be extracted, from the domestic economy. The central difference between domestic and foreign sources of savings is that domestic savings can be augmented by taxation, whereas foreign savings must be obtained at the volition of foreign governments and international institutions and of private foreign investors. Foreign official capital is obtained by governmental negotiation and is not a variable controlled by fiscal policy as such; rather, the general conduct of fiscal policy is constrained by the terms imposed by the official suppliers of foreign capital as a condition of development assistance, while fiscal policy must aim to make effective use of the extra resources provided by foreign financial assistance and to provide for interest and amortization payments on it. Private foreign capital, in contrast, is a variable subject to direct influence by fiscal policy in three major ways: through the influence of the tariff structure (and other barriers to trade) in creating an incentive for foreign enterprises to establish productive facilities in the country rather than export to it; through the influence of the general system of corporate income taxation, special investment incentives and subsidies, and so forth on the rate of return to private investment; and through the influence of special incentives or disincentives to the investment of foreign, as contrasted with domestic, capital.

Second, at the micro-economic level, the opportunity to exchange goods in the world market both

(a) enables the developing country to obtain more cheaply than it otherwise could the technologically advanced types of capital equipment and materials required for raising its level of productivity, and

(b) permits it to achieve a higher return from its development investment than it otherwise could, either by allowing it to specialize in the production of goods in which it has a potential comparative advantage in the world economy, or by giving it access to a market large enough to yield the full advantages of economies of scale.

From the standpoint of establishing a self-sustaining process of economic growth, the latter consideration is probably more important than the former. However, in practical development planning and discussions of it, major emphasis is laid on import-substitution rather than export development. The reasons for this are partly that the objective of economic development planning is usually industrialization and imitation of more advanced countries rather than raising productivity and the standard of living as such; and partly that, as will be discussed below, the balance of payments appears as a special problem of underdeveloped countries which it is easier for policy to tackle by import-substitution than by export-promotion.

When foreign trade is conceived as extending the market opportunities of the domestic economy and so permitting more profitable investment of development resources, the problems of fiscal policy with respect to foreign trade and to domestic trade are essentially the same -- to raise revenue for development and to spend it in ways that minimize private disincentives to growth and the distortion of the economy away from an efficient production pattern. From this point of view, the chief fiscal problem in development planning stems from the traditional dependence of public finance in underdeveloped countries on taxes on international trade, especially import duties. In an underdeveloped economy with only a rudimentary domestic industrial sector, taxes on exports and imports probably affect mainly the distribution of income, rather than the allocation of resources. But, as the economy develops, the allocative effects of taxes on trade are likely to become increasingly important, so that for efficiency the emphasis of fiscal policy must shift towards direct taxation, and types of indirect taxation that do not discriminate between domestic and foreign markets or sources of supply -- except to the extent that such discrimination is itself a deliberate aim of development policy, or justified by its explicit contribution to economic growth.

Balance-of-Payments Problems of Developing Countries

The external aspects of planned economic development typically appear as an overall problem of keeping the balance of payments of the developing country in balance (or not too disastrously in deficit), with the availability of foreign exchange appearing as a constraint on development policy additional to the constraint set by the scarcity of resources. Thence arises the typical concern of fiscal policy, and of extra-budgetary policy, with the balance of payments as such, rather than with the more fundamental incentive and allocative problems discussed above.

According to familiar analysis, a chronic balance-of-payments deficit may be owed, either to a chronic state of excess demand, or to an overvalued exchange rate in the absence of excess demand. Both conditions tend to be characteristic of underdeveloped economies applying programs of planned economic development, the latter increasingly so with the passage of time.

The initiation of planned economic development is itself likely to make the pre-existing exchange rate overvalued. Planned development implies both an increase in the level of domestic activity and hence in the aggregate demand for imports (and possibly also a reduction in the supply of exports), and a shift of demand towards capital goods, which have to be imported. To maintain equilibrium in the balance of payments, some reduction of domestic prices relative to world prices would be necessary, to induce shifts of resources from the domestic sector

into the international sectors of the economy (the sectors producing exports and import-substitutes). Given the inflexibility of resource allocation generally assumed to prevail in underdeveloped countries, the required relative price adjustment might be substantial, involving considerable income redistribution from consumers to producers of internationally traded goods.

Governments are understandably and naturally reluctant to contemplate such relative price adjustments and income redistributions, for various reasons. One is a specific unwillingness to reduce overtly the real incomes of the urbanized professional, mercantile, and administrative classes, to which the policy-makers belong, and of the members of the extant industrial labor force, on which they depend in part for political support. Another is a more general unwillingness to accept the writing-down of the real value of national resources that devaluation would entail. Instead, governments are prone to seek an alternative solution by direct action on the import side of the balance of payments, by means of exchange controls, quantitative import restrictions, or higher import duties. These policies are justified by reference to social priorities and to the alleged inelasticity of foreign demand for (traditional) exports and of domestic demand for (non-priority) imports.

Such actions have the effect, intended and unintended, of shifting resources into the import-substitution sector, and in part they achieve covertly the necessary reduction of real incomes in the domestic sector. But, to the extent that they constitute a tax on real incomes in the export sector, they indirectly aggravate the balance-of-payments problem by impeding rather than fostering the growth of export supply. This effect is typically reinforced by deliberate policies of increasing taxation of exports, through export taxes, discriminatory exchange rates, marketing board surpluses, and so forth. Such policies are justified either by the traditional reliance on the export industries as a source of revenue or by the argument that the demand for these exports, or the supply of them, or both, are extremely inelastic. Thus, the effort to cope with the balance-of-payments problem by other means than devaluation may result in large part in a wasteful redeployment of resources from the exporting to the import-substituting sector (wasteful because the resources are shifted from indirect production of importable goods to direct production at a higher real cost), when what is required is an expansion of both of the international sectors.

Not only is the initiation of planned economic development likely to result in the exchange rate being de facto overvalued, but the degree of overvaluation is likely to increase over time, as a result of the inflation of domestic wages and prices generated both by the tendency of economic planners to plan for an excessive level of demand, by taking overly optimistic views of the potential savings forthcoming and the

potential levels of agricultural output and increases in productivity; and by the natural tendency of wages and prices to rise in an economy operating at a higher level of activity than usual, and transforming its economic structure at the same time. The usual consequence is chronic and increasingly serious difficulty with the balance of payments, and an eventual switch of international economic policy from import-substitution to export-promotion, this policy being implemented by export-subsidies, foreign exchange "bonuses" or favorable exchange rates for export proceeds, tax incentives for export-promotion or expansion, and the like.

At this stage, the country will have achieved the equivalent of a de facto devaluation, in the sense of a similar increase in the prices of both exports and imports relative to prices in the domestic sector. The important difference from explicit devaluation is that the degree of implicit devaluation will differ among the categories of internationally traded goods, and between commodities and "invisible" items in the balance of payments, such as capital movements, tourism, and emigrants' remittances, depending on the precise nature of the policies of foreign exchange conservation and augmentation adopted. At some later stage, either the growing difficulty of administering an increasingly complex set of interventions in trade and payments -- the main purpose of which is clearly to compensate for the overvaluation of its currency -- or pressure brought to bear by the sources of external development aid (on which the country's balance-of-payments difficulties will make it increasingly dependent), will force the government to simplify the situation by explicit devaluation of the currency.

Implications for Development Policy and Fiscal Policy

The foregoing generalized account of the balance-of-payments problems and policies of underdeveloped countries that adopt programs of planned economic development is derived largely from the experience of underdeveloped countries in Asia and Latin America. It may serve as a cautionary tale from which to begin a discussion of fiscal policy and the balance of payments in a process of planned economic development. From the standpoint of formulating and conducting development policy, three major conclusions emerge from the consideration of experience.

The first and most obvious point is concerned with exchange rate policy rather than with fiscal policy, though it has an important bearing on the objectives of fiscal policy and the restrictions that may be imposed on its use for promoting development. An underdeveloped country on a fixed exchange rate which undertakes a development program and for this purpose employs the accepted techniques and instruments of planning, will inevitably develop a balance-of-payments problem. If it adheres tenaciously to its exchange rate, it will equally inevitably find itself forced to use its fiscal and other control instruments to compensate for the inappropriateness of its exchange rate. Further, once balancing the

balance of payments becomes firmly established as an object of policy, and economizing on foreign exchange an objective conditioning its use of its planning instruments, it is virtually certain that the country will come to follow policies that are different from those it would adopt if the balance of payments as such were not a pressing problem -- policies that will militate against achievements of the nominal objective of economic growth.

With respect to items in the current account, the country's policy is likely to put excessive emphasis on import-substitution -- both because imports are easier to control than exports and because the development of import-substituting industries gives the superficial appearance of economic development even if great waste of resources is involved -- and insufficient emphasis on export-promotion. Further, the criteria of saving or earning foreign exchange are likely to dictate a different choice of international sector industries for development promotion than would a calculation of comparative advantage based on relative real costs. With respect to the capital account, the balance-of-payments problem is likely to lead the country into excessive "distress" borrowing from foreign countries and financial institutions, and may lead it either to impede private foreign investment by placing restrictions on the remission of profits and capital or, at the other extreme, to provide excessive inducements to private foreign investment that promises to save foreign exchange.

To avoid having its development program fall into the balance-of-payments trap, a country ideally should adopt a floating exchange rate. The argument commonly advanced against adoption of a floating rate is that it encourages resort to inflationary means of financing development, and will, therefore, result in a continual depreciation of the exchange rate. The weakness of this objection, however, is that countries planning economic development by that very fact are under strong pressures to resort to inflationary financing, and that if they adhere to a fixed rate in these circumstances they will have to combat the resulting balance-of-payments problems by direct or fiscal means that are certain to introduce significant distortions in the allocation of resources. The choice is, therefore, not between price stability and inflation but between two methods of offsetting the adverse effects on the country's international competitive position of the domestic inflation that accompanies development planning. A floating exchange rate achieves this offsetting automatically, without interfering with the allocation of resources according to comparative advantage as modified by development planning. By contrast, under a fixed exchange rate the offsetting must be accomplished by piecemeal measures that inevitably introduce allocative distortions.

If a country, nevertheless, chooses to adhere to the fixed exchange rate system, its policy-makers should remain on the alert for the development of significant overvaluation of the currency, and be ready to

correct it by timely devaluation and to repeat the devaluation when overvaluation re-appears. This should be done rather than to resist devaluation to the last ditch, defending the exchange rate by using all the available instruments of intervention in the balance of payments, and being forced eventually into a drastic devaluation accompanied by the sweeping fiscal and monetary reforms that are almost invariably insisted on by the International Monetary Fund in such cases. In this event, there usually occurs a prolonged period of domestic deflation and heavy unemployment.

To the extent that a country does commit itself firmly to its existing exchange rate, and makes the maintenance of that rate a primary objective of economic policy, this commitment imposes the restraint of avoiding domestic inflation in its development program. Since this restraint implies maintaining sufficient slack in the economy to prevent inflation, it is a restraint that no country consciously planning economic development is likely to comply with to the extent necessary. The policy problem, therefore, becomes one of choosing a development program whose inflationary consequences on the balance of payments can be contained within reasonable limits by the available policy instruments.

In the actual conduct and formulation of policy, the chief problem for the policy-makers is to remain aware of the fact that these policy instruments are being used to offset an inappropriate exchange rate, and to design their use with reference to the underlying real economic situation rather than with reference to balance-of-payments considerations as such. For this purpose, the notion of the "shadow" exchange rate as a guide for decisions involving foreign and domestic alternatives is an essential concept for intelligent economic planning. In particular, fiscal policy affecting the production and marketing of internationally traded goods should be guided by the principle that in general the domestic prices of internationally traded goods should differ from their foreign prices by the same proportion, specifically by the proportion by which the shadow exchange rate diverges from the actual exchange rate. In other words, exports should be subsidized and imports taxed to offset the effects of overvaluation; and if the balance of payments threatens to deteriorate as a result of domestic price inflation, the policy-makers should increase the incentives for both exporting and import-substitution proportionally, rather than concentrate on increasing the incentives for import-substitution alone, as they usually do.

Deviations from the principle that exports should be subsidized and imports taxed at the same rate require economic justification on other grounds (economic development grounds) than balance-of-payments considerations. But, the budgetary problem of financing subsidies, or of achieving the effect of a subsidy on one activity by imposing taxes on the alternatives, may in practice make a divergence of domestic from foreign relative-price relationships the second-best policy solution.

The other two conclusions that emerge from consideration of the experience of development planning concern the detailed policies countries follow in attempting to keep the composition of the balance of payments in conformity with the requirements of economic development. These policies involve primarily the use of some combination of direct controls on, and taxation of, trade to restrict the overall volume of imports and to give priority to "essential" over "non-essential" imports. The "essential" imports include foodstuffs, raw materials, and capital goods; the "non-essentials" being "luxury" consumption goods and the machinery and materials for making them. The theory underlying this kind of policy is the valid principle that, if the country is to make a major effort at economic development, it must restrict its real consumption -- which in equity implies particularly restriction of consumption of luxury goods by the higher-income groups -- and invest the resources so obtained in the accumulation of capital equipment. Where the policy errs, with effects generally inimical to efficient development, is in attempting to implement this principle through action directed at limiting imported supplies of the goods in question, instead of or in addition to action directed at the distribution and disposition of the income which determines the demand for such goods.

If a country seeks to make the composition of its imports conform to the pattern appropriate to a rapidly developing economy by rationing its scarce supply of foreign exchange so as to favor imports of essential food and materials and capital goods and inhibit imports of luxuries, it is likely to impede its economic development in two major ways. Such a policy involves an implicit subsidy for imports of the essential goods, and a tax on imports of the non-essential goods, in comparison with a situation of no controls on imports coupled with an equilibrium exchange rate. By relying on foreign exchange rationing instead of imposing an explicit tax on imports of non-essentials, the policy-makers miss the opportunity to appropriate the scarcity value of non-essential imports created by rationing. Instead of adding to the tax revenue available for development, the scarcity rent is allocated to the recipients of import licenses (from whom it may be passed back as bribes to government employees) or, if domestic prices of imported goods are controlled to prevent abnormal profits, diffused among the consumers of the goods in question. This is the first deleterious effect of exchange rationing on the rate of economic growth -- the sacrifice of an opportunity to raise tax revenue. This sacrifice can be quite substantial, as is evidenced by the very high domestic prices (relative to foreign) of foreign-produced goods frequently observable in countries practicing exchange control. If exchange control or import restriction were replaced by exchange auctioning or tariffs, the government could obtain the same effects on the pattern of imports while increasing the revenues available for financing development. This is the second major point that emerges from the experience of planned economic development: that fiscal policy methods are superior to direct control methods for shaping the balance of payments to conform to the requirements of an economic development policy.

The third major conclusion regarding the adverse effects of foreign exchange rationing on economic development is one that is common with, and cannot be avoided by, the use of taxes on imports to discourage consumption. This effect occurs because a restriction or tax on imports gives an incentive to resort to substitution for imports from domestic supplies, either by giving an inducement to domestic production of the same or similar goods or by encouraging the substitution of domestic goods serving similar purposes. For example, prohibition or heavy taxation of imported items of conspicuous consumption, such as large private automobiles, may foster either the establishment of a local automotive industry or the development of conspicuous expenditure on large private residences and extensive personal services. In a very underdeveloped economy, taxation of imported luxuries may approximate closely to taxation of luxury consumption, and even restrictions or prohibitions on the importation of luxuries may reduce the consumption of higher-income groups to the benefit of savings. But, as an economy develops and becomes more differentiated, these measures are likely to become decreasingly effective as a source of development revenue (directly, or indirectly by expanded savings) and increasingly protective in effect. Similarly, the subsidies to certain types of imports implicit in unrestricted entry are likely increasingly to divert domestic resources away from the production of close substitutes, such as domestic food production or capital goods production. The consequence is that policies intended to influence the pattern of domestic expenditure, and specifically to facilitate an increase in saving and investment at the expense of consumption, come to exercise an important effect on the allocation of resources. They divert resources towards production of goods, whose import is discriminated against, and away from production of goods, whose import is implicitly subsidized.

This unintended and presumably undesirable allocative effect would not occur if taxes (or rationing, though rationing is a less efficient technique because it wastes taxable capacity) were directed at the consumption of non-essential goods rather than at the importation of them. In other words, it would not occur if the primary emphasis of fiscal policy were laid on shaping income distribution and demand to conform to the requirements of economic growth, rather than on the balance of payments as such. Taxation of consumption of non-essentials regardless of origin would be conducive to efficient allocation of resources in production, since the relative production costs of goods would be the same at home and abroad. But, taxation of goods at different rates to the final purchaser would entail some allocative inefficiency in consumption, especially in a tax system relying heavily on high rates of tax on a few major items. This is because it would induce substitution in consumption of lightly taxed for heavily taxed commodities and so promote purchases of goods having relatively high alternative opportunity costs to the economy (that is, high ratios of real cost to the country to money price to consumers). Hence, there is a case for shifting from reliance on excise and import taxation of a few items to reliance on income taxation, a general sales tax, or possibly an expenditure tax as the economy

develops. This is the third major conclusion that emerges from analysis of the balance-of-payments problems of developing countries -- the desirability of employing fiscal methods of operating on the composition of the balance of payments that do not discriminate, or discriminate as little as possible, between foreign and domestic sources of supply and among different items of consumption.

This principle of non-discrimination may seem at first sight to conflict with the earlier recommendation of a combination of import-substituting and export-promoting policies in the case of overvaluation. But, in fact, there is no conflict between the two. In the earlier case, the apparent money costs of imports and returns from exports diverge from their alternative opportunity costs as a result of overvaluation, and export-promotion and import-substitution (in parallel) are required to offset this monetary distortion of resource allocation. In the present case, taxation of imports introduces a divergence between the social opportunity costs of domestic and foreign supplies of the taxed commodities, which would be removed by taxing purchases of these commodities regardless of source. To put the point another way, overvaluation gives the country an apparent comparative disadvantage in internationally traded goods in which it has a real comparative advantage, and taxation or restriction of imports gives it an apparent comparative advantage in import-substitution where it has a real comparative disadvantage; in both cases, policy should aim at making apparent and real comparative advantage and disadvantage correspond.

Some Aspects of Import Substitution

There are a variety of reasons for expecting that the economic development of a hitherto underdeveloped country will entail the development of domestic production of import-substitutes, strictly in accordance with the principle of comparative advantage. Economic development involves the accumulation of material capital, the acquisition of skills on the part of the labor force, and the introduction of modern technology, and also enlarges the extent of the domestic market. It thus involves the overcoming of the initial comparative disadvantages of the underdeveloped country in relation to the advanced countries of the world, which make the former dependent on the latter for supplies of advanced types of consumers' and producers' goods. Import-substitution of this type may, further, have to be a deliberate objective of economic development policy, both because economic planning is necessary to ensure the efficient development of the economy and because the effects of the characteristic overvaluation of the currency previously discussed have to be counteracted by conscious economic policy.

Unfortunately, both the tendency of policy-makers to translate propositions that are valid subject to careful qualification and quantitative evaluation into simple slogans and rules of thumb, and the pressure of the balance-of-payments problem associated with an overvalued currency, typically result in import-substitution becoming an objective of development policy for its own sake, rather than a corollary of efficient allocation

of development resources. The pursuit of import-substitution as an objective in its own right can result in extremely expensive mis-allocation of resources, the costs of which to the economy are not readily apparent. Moreover, the effects of the protective policies used to encourage import-substitution on market structure and competitive conditions may be contrary to what is required for the establishment of self-sustaining economic growth. These effects are relevant to the efficient design of fiscal policy, insofar as import-substitution is implemented by tariff and taxation policies, or by direct methods (import-restriction, government investment in import-substituting industries) which could be replaced by fiscal measures that would achieve the same effect.

The cost of import-substitution to the economy can be measured by the excess of the cost of domestic production of import-substitutes over the cost of importing the same goods (corrected if necessary for the change in the exchange rate necessary to keep the balance of payments in balance). Alternatively, it can be measured by the subsidy given to the domestic producers of import-substitutes. The existence and the magnitudes of these subsidies are disguised by the fact that they are customarily given in forms that do not pass through the budget. For example, a tariff, insofar as it protects domestic production, amounts to an extra-budgetary tax on consumers and a subsidy to producers, collected directly from the former by the latter. A tax concession to firms producing import-substitutes, or government investment in the production of import-substitutes, which yields a rate of return on the capital less than the normal rate of return gross of taxes on private investment, is a subsidy at the expense of the community at large, which must pay more taxes or receive less benefits from public expenditure than it otherwise would.

A further factor which disguises the magnitudes of the subsidies offered for import-substitution is associated with the complex input-output structure of modern industry and the practice of differentiating in import-substitution policies between final assembly or manufacturing processes and the production of raw materials and components. Import-substitution policies typically concentrate on securing the establishment of domestic facilities for final manufacturing processes, and to this end both impose barriers to the importation of the finished products and facilitate the importation of components and materials. The effect of the latter practice is to make the effective subsidy offered to final manufacturing stages much higher than is indicated by the excess of the domestic price of the finished commodity over its price in the world market. Suppose, for example, that a country has a 30 percent tariff on fabricated copper products; that raw copper accounts for 50 percent of the (foreign) cost of production; and that raw copper is allowed free entry. In effect, the fabrication process is being protected at the effective rate of 60 percent. If this degree of protection is necessary to permit domestic fabrication to compete with imports, the country is incurring an excess cost of fabrication of 60 percent. This percentage also represents the excess resource cost per unit of foreign exchange expenditure saved, and the implied degree of overvaluation of the

currency (measured by the excess of the implied "shadow" price of foreign exchange over the official exchange rate). The effective degree of protection in this example is twice the degree implied by the tariff rate; much higher ratios of effective to nominal degrees of protection can easily result from combinations of incentives to import-substitution, each of which by itself may appear modest and indeed only reasonable.

The purpose of the two preceding paragraphs is to point out that the excess cost of production of import-substitutes induced by import-substitution policies is both difficult to evaluate and easy to underestimate. The implication for fiscal policy is that fiscal incentives to import-substitution need to be carefully appraised -- to determine the magnitude of the rate of subsidization implicit in them and whether the results are likely to justify subsidization at this rate. Even if import-substitution is desired for its own sake, regardless of its effect in increasing the real cost to the economy of the goods in question and in reducing productivity, there must obviously be some limit to the rate of subsidization that is justifiable. Rational policy-making should evidently attempt both to prevent the rates of subsidization offered to particular import-substituting industries from exceeding a tolerable level, and to equalize the rates of subsidization offered to the various claimants for fiscal assistance. This last proposition is frequently expressed in the recommendation that a developing country should impose a uniform (and moderate) tariff rate on imports. But, this prescription is far too simple to provide a guide through the complexities of input-output relations among industries and the effects of tax policies and concessions on the profitability of production.

Some Observations on Policy towards Private Foreign Investment

Underdeveloped countries pursuing planned economic development, and indeed all countries which suffer from a scarcity of domestic capital for investment in economic growth, typically have ambivalent attitudes towards the investment of foreign private capital in them, and especially towards direct foreign investment. On the one hand, such investment contributes to the country's growth and economic development, not only by providing scarce capital but by serving as a medium for the transmission of modern technology; recognizing these benefits, underdeveloped countries are frequently prepared to offer special tax and other concessions to foreign enterprises willing to establish productive facilities within their borders. On the other hand, national sentiment is disturbed by contemplation of the profits earned by foreigners on these investments, and also by the fact that direct investment allegedly gives foreigners "control" over parts of the national economy. Consequently, economic policy usually seeks to exercise control over such investment and its rewards by such means as insisting on resident participation in the investment, seeking to have the capital provided as fixed-interest rather than equity investment, and so forth.

The economic policy issues raised by private foreign investment are complex, and extend well beyond balance-of-payments considerations into

the fiscal treatment of private investment in general. In consequence, only a few brief observations on it will be offered here.

In the first place, a country is virtually certain to derive a substantial net benefit from foreign private investment in it. The reason is that the social benefit from such investment exceeds the private benefit to the investor in two ways. The first is by the theoretically important, but difficult to quantify, effect of investment in raising the marginal productivities of cooperant domestic factors of production and increasing the productivity of all factors by expanding the scale of the economy. The second is by the tangible and directly observable increase in direct and indirect tax revenues generated by the investment. In other words, foreign private investment in a country raises its national income by the value at market prices of the marginal product of the capital and the increase in value at market prices of the marginal products of the domestic factors it employs. The foreign investor receives only the value of the marginal product of this capital at factor cost (net of indirect taxes) less the direct taxes he has to pay to the country's government (corporate income tax, non-resident withholding tax). Cases in which a country loses by foreign investment are extremely difficult to construct: the main possibilities are that foreign investment in an export industry may increase supply sufficiently to lower the price of the export in the world market enough to reduce domestic real income; and that the profits of the foreign investor may be obtained by exploiting a monopoly position in the domestic market created by the import-substitution policies of the country. The former requires a rather special set of conditions; the latter is within the control of domestic economic policy.

It follows from the general net social profitability of private foreign investment in an underdeveloped country that, on the one hand, restrictions placed on such investment can involve substantial economic loss for the country; and that, on the other hand, there is considerable scope for a country to gain economically by offering special inducements to private foreign investors.

In the second place, from the point of view of dealing with the balance-of-payments problem, there are various reasons for preferring direct equity investment to fixed-interest investment by foreign capitalists. Direct investment brings technology and training with it, and a substantial fraction of the profits it earns is likely to be reinvested in the country more or less automatically. In addition, the profits from which earnings are remitted will tend to vary with the level of activity in the country, which in turn will reflect to some extent the strength or weakness of its balance-of-payments situation. Hence, when foreign capital takes the form of direct investment, the burden on the balance of payments of transferring payment for its services will tend to adjust itself automatically to the capacity to bear it, whereas the burden of fixed-interest charges on borrowed capital is inflexible. Moreover, if the country gets into balance-of-payments difficulties, devaluation will lighten the burden of transfers of income on direct investments, but will not affect the foreign exchange burden of fixed-interest obligations, assuming that capital and interest are denominated in a foreign currency, as they usually are.

TAXATION IN AFRICAN DEVELOPMENT

John F. Due

[From Taxation and Economic Development in Tropical Africa, Massachusetts Institute of Technology; Cambridge, Massachusetts, the M.I.T. Press, 1963, $6.00; pp. 145-163.]

[This book deals with the relationships between tax policy and economic development. Based on field research in eight English-speaking countries in tropical Africa, Professor Due analyzes in detail the effects of different types of taxes in stimulating or inhibiting economic development, and describes the special advantages or difficulties in the administration of each. Excerpts from the concluding chapter are presented here.]

These are excerpts from the book.

The key to economic growth is the transfer and better utilization of resources, not merely a shift of money. Nevertheless, financial transfers will, within the framework of the market economy, facilitate the transfer of real resources. Transfers to government from individuals -- who would spend the funds on consumption or invest them in outlets of limited significance for growth -- make it possible to obtain the factors for governmental services or capital formation without resorting to borrowing or money creation, both of which would result in competition of governmental and private spending for the resources.

The primary instrument for the transfer of funds to the government to facilitate transfer of resources is taxation. This method theoretically, at least, may also

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be used to provide incentive to increase private savings and the private-sector rate of capital formation. More specifically, in a developing economy, the tax system may be used to accomplish the following functions:

1. Curtailing consumption and thus freeing resources for governmental services or capital formation.

2. Reallocating resources from investments regarded as having little beneficial effect upon economic development (e.g., office buildings) to those of greater benefit for growth.

3. Providing a flow of funds into government hands to facilitate the transfer of resources.

4. Providing incentive to alter economic behavior in such a way as to facilitate economic growth, such as providing added incentive to save, to enter the market sector, to work longer periods, to undertake private-sector capital formation.

Regardless of the nature of the economy, there is ever-present danger that the tax system, while directly accomplishing the prime goals, may, because of its compulsory nature, have serious adverse effects upon the functioning of the economy and thus reduce national income below potential levels. This danger is particularly great in an economy with a very limited margin over subsistence and a high percentage of the population still primarily engaged in subsistence agriculture rather than in producing for market. The primary dangers are those of restricting instead of increasing the incentives to work, to participate in the market economy, to save, and to develop and expand businesses. There is particular danger that persons will find it advantageous to withdraw into the subsistence economy instead of participating more fully in the market economy.

Thus, the framing of the tax structure must give particular attention to the minimization of adverse incentive effects and maximization of incentive reactions which further the attainment of the goal. The extent to which these objectives can be attained will, in turn, constitute an important element in the determination of the optimum rate of economic growth, which cannot be defined without regard to the tax-incentive factors. Unfortunately, two major dilemmas are encountered. In the first place, the type of tax that most successfully recovers for the government a portion of the gains of the rising national income is the type that is most likely to interfere with incentives. Second, the general tax environment of an underdeveloped economy is unsuited to a high degree of perfection of the tax structure. Various significant features of such an economy include low levels of literacy and record keeping; inadequate numbers of trained tax administrators and auditors;

unsatisfactory land title situations; limited use of bank accounts; and the importance of the subsistence segment of the economy, the output of which is difficult to ascertain and value.

Income Taxation

In mature economies, the income tax is widely accepted as the most suitable primary source of revenue. The applicability of this rule to underdeveloped economies requires careful consideration. Even in such economies, however, income taxation offers several primary advantages.

In many respects, the income tax is the most effective way to reach the above-subsistence income of those groups which have attained such levels, the tax being adjusted in terms of the amount of such excess and made progressive relative to it, if desired. No other taxes can be adjusted in such a precise fashion. A large portion of the tax, under conditions such as those prevailing in tropical Africa, will be obtained from civil servants, executives and salaried employees of business firms, and professional men. Taxation of these persons will likely have few harmful effects on economic development since they are not engaged in undertaking significant business investment. The tax will recover a portion of the gains made from economic growth and particularly will catch the "unearned income" -- speculative gains, increases in land values, etc. -- taxation of which presumably has little adverse effect on economic growth. The direct burden of the tax makes persons cognizant of their responsibilities toward government. The yield is more stable than that of the major alternative sources. Finally, the tax conforms with widely accepted standards of equity.

However, income taxation in tropical Africa suffers from rather obvious limitations which, of necessity, restrict the relative reliance on it compared to the use in more developed economies. The first problem is administrative. Underdeveloped countries all suffer from a severe shortage of trained personnel for administrative work of all kinds, including income tax audit. To the extent to which this very scarce personnel is used for income tax administration, it is not available for other purposes. Other than in the top income and wage earner groups, standards of literacy and record keeping are such that accurate determination of income is virtually impossible. Application of the tax to subsistence farming income is particularly difficult because of the problems of determining the amounts and values of this income.

Inevitably, a tax which takes a certain (and usually progressive) percentage of income presumably has some effect on economic incentives. If subject to income tax, a person on the margin between subsistence and market-economy production may be driven back to the subsistence economy entirely if his market-economy income is taxed. However, as with more developed economies, the effect may be the reverse; he may seek to work

more in the market sector in order to maintain his given income from that sector. The net over-all effect is uncertain. In practice, administrative considerations dictate that persons on this margin are not subject to tax.

Similarly, it is impossible to say whether there is significant net effect on the willingness of persons to save or to undertake the risk of business development; the greater the marginal rates, however, the greater is the risk of such effects. One disadvantage cannot be challenged: an income tax provides no incentive to save more and consume less, and a relatively high percentage of tax is borne by those persons who presumably save relatively high percentages of their incomes. The tax must, therefore, be absorbed in part out of savings that would have been used for economic development. There may be no net loss from the government's absorption of this sum, but there is, at the same time, no gain so far as total capital formation is concerned; the intent of the tax program relative to economic growth has not been fully accomplished.

Thus, while an income tax has merit as an element in the tax structure of a developing economy, and its yield will grow progressively as the economy expands, the revenue potentialities are somewhat limited. In its usual form, the tax must be confined to a relatively small percentage of the population, and the rates presumably must be kept lower than would be regarded as tolerable in a more developed economy. Also, given the problems of administrative personnel, even with the limited coverage of the taxes, a maximum degree of simplification consistent with equity must be maintained.

The Personal Tax Approach

While income taxation in the usual form may be unsuitable for the mass of the population of underdeveloped economies, there is the possibility of using a direct tax of broad application, in the form of what is known in Africa as the personal tax. As the tax operates in Uganda, Kenya, and elsewhere, all persons (or, typically, all adult males) are subject to a minimum tax, and those with higher incomes are assessed on a graduated scale, up to a maximum figure that is reached roughly at the level of income at which the income tax becomes effective. Assessment is usually made on a local basis, by a committee of county and village officials (in Uganda) or nonofficials who are familiar with local conditions. For employees, the tax is based on actual income; for the typical semisubsistence farmer, it is based on external criteria of probable income such as acreage and number of cows. Non-Africans are usually assessed at the maximum unless they file a return to demonstrate lower income.

In Eastern and Western Nigeria, the personal taxes are included in the income tax structure, the latter extended by a minimum tax rule down

to the lowest income groups. The portions of the taxes applying to the lower income levels are, however, administered in much the same fashion as the personal taxes of other jurisdictions.

On the whole, the operation of these personal taxes appears to be satisfactory, and the experience confirms the possibility of using mass direct taxes in underdeveloped economies. While only rough equity is attained in assessment, the results appear to be reasonably good, and enforcement standards are usually high; certainly there is no mass escape, as evidenced by the numbers of taxpayers relative to the total population. Administration is largely in African hands. The principle of direct taxation is firmly established, reliance on indirect taxes is reduced, and, in time, the taxes can be perfected so far as equity is concerned.

These taxes have two potentially beneficial economic effects. Since the taxes must be paid in money, they force the subsistence farmers to sell produce or labor services. The graduation does not become effective for the great mass of the farmers at the subsistence margin; for those who are affected, there is less danger that the tax will drive them back to greater emphasis on subsistence farming. Secondly, so long as a person remains in the same tax bracket, he has incentive to earn more, not less, since the additional income gives rise to no added tax liability.

There is some danger at the bracket points, where the marginal rate often exceeds 100% as the person moves into a higher bracket, and thus he may be discouraged from gaining added income. But once he is in the bracket, he again has incentive to earn more, not less. Furthermore, to the extent to which assessments are based on potential rather than actual income, incentive is given to work harder. This rule, however, may violate usual standards of equity.

Corporate Taxation

In an underdeveloped economy, the tax potential from corporations usually exceeds that from individuals at typical rates. In such economies, a substantial portion of potentially taxable income is earned by a relatively small number of companies, often foreign-owned, and failure to tax their net income would allow a large portion of the potential tax base to escape. However, it is, of course, obvious that heavy corporate taxation can interfere with economic growth, both by taking funds which would be used for expansion and by lessening the incentives to expand. The magnitude of the adverse effect cannot be defined, but the dangers are such as to require caution in the use of the taxes. There is, however, the possibility that appropriate adjustments in company taxation may be helpful in attaining better use of resources in economic development.

First, because of these considerations, there is justification for holding the tax rates below those tolerable in the more developed

economies. This has been the practice in the eight African countries, although the rates, in the range of $37\frac{1}{2}\%$ to 45%, are not far below those of the mature economies.

Second, so far as domestically held companies are concerned, there is merit in avoiding double taxation of dividend income -- much more merit than in a highly developed economy. The African countries in the past provided complete credit at the dividend level for tax paid at the company level; all continue to do so on their basic company taxes except Ghana, while the East African countries now levy a supplementary 10% corporate tax for which no credit is allowed.

Third, special tax concessions to new or expanding industry may greatly reduce the potential adverse effect of the taxes upon company expansion, and also upon the expansion of smaller noncorporate businesses, to which the same rules usually apply. These concessions take two forms: general provisions applicable to all firms; and those granted only to specific firms upon request, under what is generally known as pioneer-companies legislation.

One major general concession is the establishment of very liberal provisions for loss carry-forward, so that new firms or expanding firms that suffer losses in the first few years of operation will obtain subsequent tax reductions. Nigeria, Rhodesia, and the East African countries all permit unlimited carry-forward of losses; the period is limited to six years in Sierra Leone and 15 years in Ghana. A great advantage of this approach is that the risk of developing new enterprises is materially reduced, yet the actual relief is confined to the firms that need it, and the amount of the relief is dependent on actual losses and thus on need.

A second type of general concession is that which allows accelerated depreciation or, in other words, a very rapid write-off of new capital equipment in the early years of investment. This is particularly important for expansion of existing profitable businesses; the risk from the expansion is reduced, a tax-free loan in the form of deferment of taxes is provided, and so long as the company continues to expand, there is a net tax saving. The programs take two forms: initial allowances, in which the additional allowance in the first year reduces those in subsequent years, and the investment allowance, in which the additional amount in the first year does not reduce subsequent allowances. In developing economies, such allowances offer significant potentialities without the administrative problems created by tax holidays, as noted below. The initial allowances encourage long-term capital investments more than other approaches, although in so doing they give particular advantages to capital-intensive techniques, which may be regarded as undesirable in labor-surplus economies.

In reverse, if the government wishes to check investment along certain lines, it can deny the use of the special allowances in these fields,

and even the deductibility of any depreciation charges. This policy has been followed to some extent in the African countries by adjusting the rates of the allowances according to the relative importance attached to the particular category of investment.

The pioneer-companies or tax-holiday type of legislation authorizes complete exemption from tax for a period of years, usually five, for new firms upon specific request and approval. In Africa the practice is confined to the three West African countries and is regarded as objectionable in East Africa and Rhodesia.

The experience of the West African countries indicates clearly the difficulties of this approach for encouraging economic development. The greatest difficulty has been the long delay in processing applications, often from five months to a year. More speedy handling would require additional personnel, and they are very scarce. A related difficulty is that of establishing clear-cut criteria for decision on the applications; neither Ghana nor Nigeria has solved this problem. Nominally, priority has been given to firms using primarily domestic materials and personnel, to those with large numbers of workers, and to those which appear to make a major contribution to economic development, in contrast, for example, to breweries or bottling plants. But the latter types are the ones which frequently make application and not infrequently are approved because of their indirect contribution to the development of a skilled labor force.

There are other difficulties as well. The gains to the firms from the concessions are sometimes offset by requirements as to location of plant and other factors imposed as conditions. There is also the question of renewals; if a firm insists that it must have an extension of the concession at the end of the five-year period, the government may be reluctant to deny it.

Finally, there are grave questions about the significance of the concessions for investment policy; at best, they represent merely one element in the picture. It is often argued that the advantage is mainly psychological; the concession is a symbol of favor toward private enterprise. But even this may be offset by other government policies, as it has been in large measure in Ghana.

Thus, the basic issue in the choice of the two methods is this: a program adjusted in light of the situation of the individual firm can, in theory, be most suitable in preventing the income tax structure from deterring investment, and in directing investment along the most desired lines. However, this approach gives rise to serious problems of implementation, problems difficult in any economy, and particularly in those in which competent administrative personnel are extremely scarce. This suggests that a general program of tax relief via loss carry-forward and accelerated depreciation is more suitable under the circumstances than

pioneer-companies legislation, with perhaps some adjustment by general rule of the rate of acceleration according to the estimated contribution of the general line of activity to the economic development program.

Indirect Taxation

In view of the potential conflict of income taxation with the incentives important for economic development, the desire to encourage savings at the expense of consumption, and the administrative problems of income taxation, it is widely argued that indirect taxation should play a major role in the tax structures of developing economies. In fact, of course, they typically do. In the eight African countries, customs and excises yield over 40% of the revenues in all of the countries except Rhodesia, and over 60% in five. From an economic standpoint, the primary argument for indirect taxes is that they are not directly related to the earning of income and thus, unlike income taxes, do not constitute a disincentive to earn monetary income. At the same time, since the indirect (commodity) taxes raise the costs of consumption relative to saving, incentive is provided to increase the percentage of income saved. By concentrating the burden upon persons spending high percentages of their incomes, it is argued that these taxes force greater reduction in consumption per dollar of revenue than does the income tax. If the taxes are imposed primarily upon luxury goods, not only can curtailment of luxury consumer spending be maximized, but reasonable accord with usual standards of equity can be attained. Basic subsistence expenditures can be freed of tax.

Furthermore, since the consumption taxes in developing economies apply primarily to imported goods, they can be used to curtail luxury spending on such goods and thus lessen foreign exchange difficulties which are often encountered with rapid growth, and free foreign exchange for industrial goods needed for economic development. The final major argument for indirect taxes is the greater ease of administration, since the taxes can be collected from the importer or large producer. It is for this reason, more perhaps than any other, that colonial tax systems from the earliest days concentrated on customs duties, and movement away from them has been slow.

These arguments obviously have some merit. But there are conflicting considerations as well. The effectiveness of the taxes in reducing consumption is weakened to the extent to which savings are made to buy goods in the future, and it is expected that the tax will be permanent. While it is true that the indirect taxes do not directly impinge on income, they do affect the utility of the income. In countries moving from a very undeveloped state, money income is desired by the mass of the population directly and immediately for the goods that can be obtained with it. Thus, to the extent to which these goods are taxed and made more expensive, the effect is the same as if the tax were imposed directly

on income. Whether there will be a net increase or decrease in effort depends upon the relative importance of the income and substitution effects; but under such circumstances the net effect will differ little from that of an income tax. Duties on articles of widespread consumption may simply encourage persons to go back into the subsistence economy; very high taxes on luxury goods, such as the Ghana purchase tax, may shift purchases to other goods, materially impair incentives, and produce a hostile popular reaction. Certainly in Ghana and British Guiana, there were violent reactions to the sharp increases in taxes, to the detriment of political stability and economic growth.

Closely related are equity matters relating to the selection of commodities to be taxed. If a limited number of luxury goods are subjected to high rates, discrimination against the persons preferring these goods over substitutes is inevitable. If significant revenue is to be obtained, items of wider consumption are required, and equity considerations again arise. The tax must of necessity be collected at the time of importation or basic manufacture, and pyramiding of the tax burden plus unequal burden on various lines of consumption because of varying distribution margins are inevitable. With customs duties, the task of constructing tariffs that accomplish the desired ends is difficult. Moreover, high rates will encourage smuggling, already a problem of some magnitude in Nigeria and other countries. It is likewise difficult to keep producers' goods free of customs duties unless they are highly selective, and the cost of investment is artificially increased. A basic difficulty is created by the "catchall" categories in the tariffs. If there is none, any item not falling within a defined category is duty-free, and discrimination and loss of revenue result. If there is one, some producers' goods will almost inevitably be caught at relatively high rates.

This discussion of indirect taxes is based upon the assumption that they are shifted forward to the consumers of the products. As is well known, there are, without question, exceptions to this rule. With customs duties and flexible exchange rates, the duties may alter the rates, and thus the distribution of the tax burden will be materially altered. These complications destroy, in part, the characteristics of the tax as a levy related to consumption and result in greater similarity between the indirect taxes and a haphazardly distributed income tax.

Export Duties

A characteristic feature of many underdeveloped countries is the export of basic materials, such as farm products or ore, often primarily of one or a few commodities. Exports are frequently channeled through a governmental or semigovernmental marketing board. Under such circumstances, governments typically levy export duties, either as a fixed amount per physical unit or related to price. The effect, at

given exchange rates, is to reduce the net income of the producers of the basic products. Such duties have several advantages. World prices of these basic products often fluctuate substantially; in good years the governments can obtain large sums of tax revenue for use in economic development and, at the same time, cushion the economy from the inflationary effects of the sharp rise in incomes of the producers not accompanied by an increase in domestic output of consumption goods. Since the base of the levies is physical output or gross price, it is argued that they have less effect in restricting production than would income taxes imposed upon the net earnings. Administration is very simple so long as marketing boards are used.

However, there are major objections to this form of tax. The primary one, as stressed by P. T. Bauer, is that such taxes, since they are directly related to output and apply to all producers, small and large, do have serious adverse effects in reducing output of the products and thus retard economic growth. The typical income tax applies only to the higher-income groups; the export duties hit the small producer on the margin between subsistence and market farming. To many students of the question, this consideration is so important as to outweigh all others. The taxes are also discriminatory against the producers of those crops subject to tax, and inevitably there will be some shifting of resources from these crops to others, or to greater production for the domestic market. From an equity standpoint, it is difficult to justify the imposition of particularly heavy taxes on the producers of certain goods and not on others. It should also be noted that revenues are highly unstable.

Taxation of Land and Other Property

Of all forms of taxation, that on land offers the least danger to economic development per dollar of revenue obtained. Moreover, taxation of other forms of property is potentially less dangerous than forms whose impact is initially on income or immediate uses of income. Rapid economic growth, with its accompanying expansion of metropolitan areas, brings sharp increases in land values, which reflect economic rent. This is a surplus return unnecessary to make factor supplies available for use. Taxation of these rapidly increasing land values will have no effect upon the development, but will lessen the burden of other taxes and has substantial merit from an equity standpoint in checking the growth of large fortunes from land speculation. Taxation of land differs from taxation of income from land in two ways. First, idle or underutilized land is taxed much more effectively by the former. Second, there is no direct connection between the amount of the land tax to be paid during the year and the income earned. The lump-sum nature of the land tax, once assessed, is an incentive to greater and more efficient production, whereas income taxation or export duties may have the opposite effect.

Moreover, taxation of other property -- buildings, motor vehicles, and the like -- offers less danger to incentives than levies directly related to the earning and use of income. Application of moderate taxes to buildings in urban areas has added justification on the benefit principle, since the construction of the buildings is directly responsible for additional municipal services.

Unfortunately, however, in many underdeveloped areas of the character of the tropical African countries, there are serious limitations in the way of effective use of property taxes. In West Africa, and to a considerable extent in the other countries as well, there are no registered land titles, except in a few cities, and essentially no private ownership, except of some urban land. In some areas, even, for example, in Ghana, there is still a substantial amount of nomadic agriculture, with persons moving on to a new site in the jungle as the present plot loses fertility. Even in many cities, such as Accra, there are no cadastral surveys or title registry, or clear titles of ownership. As a consequence of these conditions, there is no taxation of rural land at all (with the exception of a low rate tax on some farm land in Uganda). Urban property taxation is confined to improvements in the Ghanaian cities and to annual rental value (with no taxation of unimproved land) in Lagos and a few other Nigerian cities. In Kenya and Tanganyika, however, where urban land titles are clearly defined, there is taxation of land values in the urban areas, with improvements free of tax. In Uganda and Rhodesia, both land and improvements are taxed, but the former at a much higher rate. In the rural areas the occupiers do not pay rent for the use of the land.

While the African countries do not have the large land holdings problem characteristic of some underdeveloped countries, the general field of land taxation offers perhaps the greatest opportunity for improvements in their tax structures. However, before this can be accomplished, registry of rights of ownership or use of land and land surveys are required. Since in many instances there are no land sales, figures of land values must be built up through classification of land by use, fertility, etc., and ascertainment of potential income. If farm product prices fluctuate sharply or substantial inflation occurs, a workable system for revision of land values is imperative, or the relative contribution of the land tax to over-all revenues will not be maintained. When the land is not owned by the individual, but the latter has occupancy rights, the levy may technically be called a rent, but the effect will be exactly the same as if it is designated as a tax.

REPORTS ON PROBLEMS OF TAX REFORM IN LATIN AMERICA

The Organization of American States (OAS), the Interamerican Development Bank (IDB) and the United Nations Economic Commission for Latin America (ECLA) are conducting a joint program of research, conferences and publications to promote the reform of tax systems and the improvement of tax administration in Latin America. Two major conferences have been held and the papers and proceedings have been published in Spanish and will be published in English. In addition, a number of studies of the tax systems of selected Latin American countries are in process of preparation.

The first conference was held in Buenos Aires, Argentina, in October 1961, and dealt with the problems of tax administrations. The Conference was attended by 66 experts, who served either as participants or observers, from 18 countries that are members of the sponsoring organizations plus Canada and Israel. Papers were presented and discussed on common obstacles to effective tax administration; estimating the distribution of the tax burden; statistical records for the management and control of tax administration; automatic data processing and tax administration; trends in management techniques; accounting, auditing and knowledge of business practices in relation to tax administration; controlling income tax evasion; administrative criteria in the establishment of sales and excise tax structures; and concepts and administration of taxes on property.

The second conference was held in Santiago, Chile, in December 1962, and was concerned with the relationships between fiscal policy and economic growth. It was attended by 70 experts on fiscal policy and top-level officials responsible for fiscal policy in the member countries. The papers and discussions dealt with fiscal policy in Latin America's economic development; fiscal capacity of developing economies; the

role of taxation in economic development; issues of tax reform for Latin America; public expenditures and economic development; personal income tax in Latin America; taxes on net wealth, inheritance and gifts; corporate income taxation in Latin America; production and consumption taxes and economic development; reform of agricultural taxation to promote economic development in Latin America; and fiscal problems in relation to a common market.

The papers and proceedings of the two conferences will be published in English by the Johns Hopkins Press, Baltimore, Maryland, by the end of 1964. The Spanish editions have already been published by the Pan American Union under the following titles:

Reforma Tributaria Para America Latina:
I, Problemas de Administración de Impuestos;
Programa Conjunto de Tributación, OEA/BID/CEPAL;
Washington, D.C., Union Panamericana, 1963,
vi y 546 pp., US$3.00.

Reforma Tributaria Para America Latina:
II, Problemas de Politica Fiscal, publicado
bajo la dirección de Alvaro Magaña (OEA),
James A. Lynn (BID), Marto Ballesteros (OEA),
Programa Conjunto de Tributación, OEA/BID/CEPAL;
Washington, D.C., Union Panamericana, 1964,
vi y 845 pp., US$4.00.

TWO CURRENT PUBLICATIONS FROM
THE INTERNATIONAL PROGRAM IN TAXATION
OF THE HARVARD LAW SCHOOL

Bird, Richard and Oliver Oldman, editors, Readings on Taxation in Developing Countries; Baltimore, The Johns Hopkins Press, August 1964, viii and 556 pp., US$8.95.

This is a most useful set of readings covering the main aspects of fiscal policy and taxation in economic development. Seven major sections deal respectively with fiscal policy and economic development; comparative fiscal systems; income taxes; sales and expenditure taxes; local finance and real property taxes; taxes on foreign trade; and regional integration, tax administration, and technical assistance. Each section contains reprints of or long excerpts from articles, monographs, and chapters of books by recognized experts, governmental commissions, and World Bank Mission reports. These selections are self-contained, including their original footnotes and bibliographical references. Each section is prefaced by comments of the editors. The volume concludes with a selected and briefly annotated bibliography for further reference.

Richard Bird is assistant director, Research Program on International Economic Integration, Columbia University; Oliver Oldman is professor of law and director of training, International Program in Taxation, Harvard Law School.

Heller, Jack and Kenneth M. Kauffman, Tax Incentives for Industry in Less Developed Countries; International Program in Taxation, the Law School of Harvard University, Cambridge, Massachusetts, 1963, xii and 288 pp., US$4.50.

This study examines both the legal and the economic aspects and implications of the various types of tax incentives granted by developing countries to stimulate private investment, local and foreign, in the development of

industry. Based upon empirical research and technical analysis, the authors conclude that the importance of tax incentives in investment decisions has generally been exaggerated. In addition to describing the various types of tax incentives used by developing countries, the study analyzes their legislative and legal characteristics; explains the methods by which their economic effects can be measured; and compares the relative advantages and disadvantages of each of the main tax incentives.

This report completes the current phase of research and publication on taxation in the developing countries of the Harvard Law School International Program in Taxation. Previous publications and conferences of the Program have dealt with various aspects of agricultural taxation and of the taxation of foreign investment.

FOSTERING PRIVATE ENTERPRISE IN DEVELOPING COUNTRIES

The advantages and difficulties of developing local private enterprise, and the policies and programs required for doing so, have received comparatively less attention in development research than have other aspects of the development process. Yet, if developing countries are to achieve their economic and social objectives, the growth of types of private economic initiative and activity appropriate to their needs and cultural backgrounds cannot be neglected.

The two studies summarized in this section analyze the problems and possible methods of stimulating Africans and Latin Americans to increase and improve private economic activities in manufacturing and extractive industries, wholesale and retail distribution, and the service trades. They focus particularly on what can be done in these respects by local entrepreneurs themselves, by their governments, by foreign private business firms operating in their countries, and by foreign governments and international organizations through appropriate assistance programs. These studies were prepared and published by the National Planning Association under the research program of the Office of Research and Analysis, U.S. Agency for International Development, by means of a contract between the U.S. Department of Commerce and the National Planning Association.

This section concludes with a description of a new catalog of investment opportunities in the developing countries for the use of prospective investors, local and foreign.

THE DEVELOPMENT OF AFRICAN PRIVATE ENTERPRISE

Theodore Geiger and Winifred Armstrong

[The Development of African Private Enterprise, by Theodore Geiger and Winifred Armstrong; Washington, D.C., National Planning Association, 1964, ix and 158 pp., US$2.50.]

This is a summary of the study.

The past hundred years of European colonial rule brought about a decisive break with Africa's traditional past and, with the coming of independence for more and more African nations, a radical transformation of African societies and economies is now irrevocably under way. One main aspect of this transformation is the achievement of economic development by means appropriate to African conditions and aspirations. One major means for achieving African economic and social development is through the encouragement of modern forms of private economic initiative and activity on the part of Africans.

By encouraging such indigenous private enterprise, the nations of tropical Africa can accelerate the achievement of national development goals and lessen their present economic dependence on foreign capital and skills. The expansion of African private enterprise will create additional employment opportunities. Private enterprise gives more individuals greater incentive to make better use of their savings, time, equipment, materials, and labor than does state-owned enterprise. Under conditions of healthy competition, private enterprises are also more likely to adopt technological

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and managerial innovations and to take advantage of new economic opportunities -- two essential aspects of the process of development.

These potential benefits of private enterprise are likely to be realized only with the assistance of the African governments, which must plan for the total growth of the economy and aim to maximize the contribution of the private sector within this framework.

It is the government which must provide the infrastructure -- the power, water, transportation, and communications -- essential for all development. In addition, the African private sector will develop rapidly only if government policies and programs provide the economic incentives and the financial and technical assistance required to expand and improve its operations.

This study analyzes the main problems which impede the emergence and development of modern forms of indigenous private economic activity in the 37 countries of tropical Africa, and describes the measures which could be undertaken by African entrepreneurs themselves, by their governments, by the foreign private companies operating in Africa, and by foreign governments and international organizations providing aid to African countries. Research was concentrated on eight independent countries in various parts of Africa whose problems relating to African enterprise are representative, and which are of particular interest because of their varying recent political and economic experience -- Ghana, the Ivory Coast, Kenya, Liberia, Nigeria, Senegal, Tanganyika, and Uganda.

African Economies Today

Despite the economic, cultural, and political changes now under way in Africa, the major portion of the population is still engaged in agricultural and pastoral activities, largely for subsistence purposes. Despite its rapid growth in the past two decades, the market economy in most African countries still does not involve more than 10 percent of the population on a full-time continuous basis; in addition, a rather higher percentage may be working for wages or producing agricultural exports on a part-time or intermittent basis.

The distribution of African enterprises, outside agriculture, reflects the relative capital and skills required for various types of economic activity. By far the greatest number of African enterprises are in retail distribution which, along with the service trades, requires the smallest capital, makes the simplest demands on technical and managerial capabilities, and is closest to traditional occupations. There is a profusion of small retailers in most countries, often too many for their ventures to be profitable. So far, only in Ghana and in Nigeria are there substantial numbers of Africans engaged in wholesaling and foreign trade. Service and artisan activities, the next

largest group of African enterprises, range from carpentry, shoemaking, and tailoring to law, accounting, and newspaper publishing. Transportation and construction probably engage the third largest group of African entrepreneurs. African-operated manufacturing activities are limited, with few exceptions, to Ghana and Nigeria. They include firms making textiles and clothing; furniture, mattresses, radios, luggage, plastic products; soap, cosmetics, and perfumes; soft drinks, tires, gravel and special clays; and other light consumer goods and construction materials. The smallest field of activity for African entrepreneurs is banking and finance, although Africans have participated in establishing successful banks in Nigeria and Liberia.

The distribution of African entrepreneurial activities is also affected by geographical and historical considerations. In general, they are larger scale and more complex in the coastal than in the inland countries, and in those formerly under British rule than in those formerly under French rule.

Characteristics and Problems of African Entrepreneurs

The African entrepreneur lives in two worlds -- the one traditional, the other modern.

In Africa, as in other traditional societies, the primary obligations are to the family as a basic social unit, and the family can extend to literally dozens of people. These traditional family obligations require that African entrepreneurs provide jobs for their relatives; they also may strengthen African reluctance to enter into partnerships with nonmembers of the family or tribe, or to entrust such outsiders with important responsibilities. The casual economic transactions of the traditional society have not prepared African entrepreneurs for the modern discipline and planning required to fill orders by a specified time, in specified quantities and qualities, and at fixed prices.

While these social impediments to the growth of African enterprise are largely beyond the reach of deliberate government policy measures, the economic characteristics and problems of the entrepreneurs are in the main susceptible to policy measures applied by governments and by private enterprise itself.

One major economic problem is lack of adequate capital and credit. With few exceptions, commercial banks have not yet begun to play an important role in financing African private enterprises and the foreign banks have tended to reserve their funds for the export trade and the local branches and subsidiaries of foreign firms. African enterprises often suffer from a shortage of working capital even more than from an inability to obtain additional investment capital. This arises partly

from the scarcity of short- and medium-term credit available to Africans. But, in many cases, it is also the consequence of undercapitalization of the enterprise itself and lack of knowledge about the continuing and contingent expenses for which the entrepreneur must plan.

Inadequate skills constitute a more serious, though less intractable, problem than inadequate capital, for skill can often substitute for capital and is in itself a major source of increased productivity and growth. In particular, few Africans have the managerial training and experience required to plan, allocate, and record their use of funds, equipment, supplies, and labor. It has been estimated that more than 90 percent of small African entrepreneurs keep inadequate records or none at all.

A market demand of small size and sporadic character and a shortage of "middle management personnel" are further problems which African entrepreneurs have to face.

The practice of mutual aid and cooperation, characteristic of traditional African societies, can be, and is being, utilized by African entrepreneurs to arrange for joint purchasing and other common services, provide a framework for establishing credit, and share information to overcome inadequate skills and inefficient methods. Cooperative and trade (joint service) associations can obtain loans and credit more easily than an individual, and can make bulk purchases of materials and operating supplies. They can also make collective efforts in marketing, publicity, practical research, and representation to government authorities. Nation-wide associations of distributors handling similar goods could be organized into a network of agents and distribution outlets able to attract distributorships of overseas manufacturers. Without such a network, African wholesalers and retailers have had difficulty in obtaining bank credit and providing the distributive facilities necessary to attract foreign manufacturers, who have generally given their distributorships to non-African firms.

The Role of Foreign Companies in Stimulating African Entrepreneurship

Foreign private investment in Africa can look forward to a reasonably secure and prosperous future as and if it becomes part of a larger and equally vigorous indigenous private sector. Except for commercial agriculture, the bulk of modern economic activity in Africa today is in the hands of African governments and private foreign companies. A perpetuation of this disproportion would not be conducive either to the most dynamic form of African development or to the future welfare of foreign firms.

In general, foreign firms can encourage the growth of African enterprise by: 1) seeking out African suppliers who can provide goods

and services needed by the company, and working with these entrepreneurs to help them improve their capacity to meet standards of modern business performance; 2) adopting policies for training and promoting qualified African employees; 3) cooperating -- in the case of foreign banks and financial institutions -- in programs designed to increase African savings and to provide long-term credit facilities to African entrepreneurs; 4) promoting entrepreneurship through joining and strengthening African businessmen's organizations and encouraging equity investments by Africans.

The Role of African Governments in Stimulating African Entrepreneurship

The influence of African governments, which have the most to gain through the growth of indigenous private enterprise, is of paramount importance. Governments, particularly in the French-speaking countries, which have assigned a comparatively minor development role to indigenous private enterprise, should re-examine their development strategy to seek ways of enabling Africans to initiate enterprises, which will contribute to the growth of the country. Specific development priorities in and among the various sectors and government policy with respect to the future role of public enterprise should be stated, in order to provide both indigenous and foreign private entrepreneurs with guidelines required to make their own plans. Governments engaged in comprehensive development planning should provide for active participation of the private sector in the planning process.

African governments should: 1) accelerate their present efforts to improve financial assistance programs by requiring better defined lending procedures and concentrating on entrepreneurs of proven ability; 2) expand in size and scope the technical assistance and training programs for entrepreneurs and their employees; 3) improve educational systems to provide more vocational training at primary and secondary levels, and to increase specialized financial, technical, and managerial training at secondary and advanced levels; 4) encourage African private enterprise, as and when it becomes capable of doing so, to purchase government-sponsored enterprises initiated at a time when private entrepreneurs were unable to start such industries themselves, thereby releasing government capital for additional productive investment; 5) require public enterprises, whenever feasible, to utilize indigenous entrepreneurs as suppliers of goods and services.

Foreign Aid Programs Affecting the Development of African Private Enterprise

Capital obtained from foreign governments, international organizations, and private foreign investors has provided from one-third to one-half of development investment in tropical Africa in recent years. With the exception of the aid programs of the United States and Israel, a

large part of foreign government and international organization assistance supports the establishment or expansion of public enterprises, which operate either separately or jointly with foreign private enterprises, while the programs for assisting African private enterprise remain inadequate. In considering African requests for foreign aid, the question of whether or not the recipient operating agency is to be a public enterprise is as important as other review criteria, such as economic feasibility, contribution to economic growth, technical soundness, and market demand.

It would be desirable for foreign governments and international organizations to re-examine the distribution of their aid funds and personnel among the various sectoral programs to ensure that the proportion of aid devoted directly to assisting African private enterprise is adequate to enable African entrepreneurs to benefit to the fullest possible extent from the proportion devoted to infrastructure, agriculture, and other fields.

Other ways in which the United States and other foreign assistance agencies might improve their direct aid to African entrepreneurs include: 1) expanding and improving government programs providing help to African government agencies and financial institutions making loans to, and equity investment in, private enterprise, and to programs providing help to African government technical assistance and training activities for entrepreneurs and their employees; 2) extending help given to African countries in designing studies of future manpower requirements for both the private and public sectors; 3) initiating a program for providing technical and business advisers for African entrepreneurs, possibly utilizing retired businessmen from the developed countries.

THE DEVELOPMENT OF
LATIN AMERICAN PRIVATE ENTERPRISE

Frank Brandenburg

[The Development of Latin American Private Enterprise, by Frank Brandenburg, with an Introduction by Theodore Geiger; Washington, D.C., National Planning Association, 1964, xii and 136 pp., US$2.50.]

This is a summary of the study.

Latin American private enterprise can make a crucial contribution to economic growth and especially to democratic evolution in the countries of the region. Not only are private firms generally more efficient than public enterprises; they are also more apt to introduce innovations and to expand their operations where opportunities arise. The evolution of democracy is even more sensitively dependent on individual self-reliance and decentralized, private decision making. Given the long history of violent, authoritarian, and extremist politics, the development of private business, along with independent farm, labor, professional, and other private groups, is especially important in Latin America.

The study examines private entrepreneurship in Latin America as a whole; however, it is focused particularly on industrial entrepreneurship in the six Latin American countries which account for 85 percent of Latin America's gross product -- Argentina, Brazil, Chile, Colombia, Mexico, and Venezuela.

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What Latin American Entrepreneurs Can Do for Themselves

There are many ways in which Latin American entrepreneurs can contribute to the development of their communities. In an effort to help identify them, a survey of over 500 businessmen was carried out. The survey reveals that business ownership in Latin America derives from an unusually wide spectrum of sources, financial as well as cultural.

Despite the varied origins of Latin American business ownership and a rate of ethnic assimilation of various groups generally high in comparison to other parts of the world, there is a recognizable pattern of life deriving in large part from the prevailing Iberian background. An important element derived from this background is the strong emphasis on family loyalty which often leads to the exclusion of outsiders from responsible positions, no matter how much they might benefit the family firm. The sharp distinction between social friends and business friends reinforces this form of exclusiveness. This attitude is not conducive to the establishment or expansion of employee training programs in the older type of enterprise.

The business community's relations with labor unions are also hampered by these traditional attitudes. As a result, labor organizations have concentrated on obtaining concessions through legislation. Businessmen protest that much of this legislation is advanced even by Western European or U.S. standards; they say that welfare costs are eating up the profits which might otherwise be devoted to improving the physical plant and to new investment.

As far as government-industry relations are concerned, businessmen also object to the spread of state-owned corporations, with their high costs, low output, and administrative favor. They point to the frequency of graft among officialdom. In general, businessmen are on poor terms with their governments and are relatively inactive politically.

Restrictive attitudes and policies of both entrepreneurs and governments, along with other hard realities, are reflected in prevailing lower profit levels in Latin America, in contrast to Western Europe and the United States. After-tax net profits, as a percent of total capital employed, were as follows for 41 locally owned business firms in five South American countries: 1958 -- 12.58%; 1959 -- 13.94%; 1960 -- 13.58%; 1961 -- 11.44%; 1962 -- 10.41%. These figures suggest an element of mythology in the picture of huge fortunes to be made in Latin America.

The small scale of manufacturing enterprises means that they often lack the credit, merchandising, and servicing facilities to compete in international markets. Only in the Central American Common Market has there been any real progress toward a preferential expansion of intraregional trade. A similar preference system is now planned for the

Latin American Free Trade Area, where a series of industry-by-industry "complementation" agreements is being worked out.

Latin American entrepreneurs will serve their own best interests, as well as those of national economic and social development, if more of them will: 1) emphasize increased efficiency, lower unit costs, improved products, and lower prices; 2) acquire competence in modern management techniques; 3) give employees greater opportunities for educational, managerial, and technical training; 4) accompany these training programs with encouragement of employees to take on increased responsibilities in management and plant supervision; 5) consider the positive gains of broadening stock ownership; 6) assume greater participation in politics and development planning; 7) identify themselves and their industries with local community development; 8) recognize that attacks on responsible foreign private investment may have adverse consequences for domestic private capital; 9) accept the framework of the Alliance for Progress as the only probable alternative to state socialism and totalitarianism.

What Latin American Governments Can Do

The spread of nationalized industry is the largest single problem in governmental relations with private enterprise in Latin America. Other problem areas, such as taxation, labor legislation, and controls, have been extensively discussed in other recent publications. The present study analyzes particularly the difficulties caused by the high proportion of government corporations.

For this purpose, a list of the 30 largest firms in Argentina, Brazil, Chile, Colombia, Mexico, and Venezuela was compiled. The distribution of ownership between governments and local and foreign private capital is given for each firm. In simplified form, the totals for the 30 largest enterprises are as follows:

	Government	Domestic Private	Foreign Private
Argentina	61.3%	20.5%	18.2%
Brazil	59.1	20.0	20.9
Chile	63.3	18.0	18.7
Colombia	54.1	39.1	6.1
Mexico	82.2	13.9	3.9
Venezuela	74.0	22.9	3.1
TOTAL	65.7	22.4	11.8

Development banks afford a channel through which governments can and do assist business to develop needed industries. These banks exist in various forms in each of the six countries. They vary considerably

in policy: Nacional Financiera in Mexico provides an example of a development bank that has uninterruptedly placed relatively low priority on loans to private industry in contrast to its large commitment of resources to state enterprises; Corporación Venezolana de Fomento-Banco Industrial de Venezuela has introduced direct financing of private industry; COPEG, in the state of Guanabara, Brazil, offers an unusual example of a state bank working almost exclusively in the field of lending to private enterprise. The Inter-American Development Bank and the U.S. Agency for International Development are providing additional financing for banks of this type.

National development planning is another means by which governments could promote development without assuming ownership and management themselves. In Latin America, however, development planning, as interpreted by some governments, has become yet another weapon of bureaucratic expansion and has virtually excluded effective participation by the private sector. Of the few attempts to bring private enterprise into the planning process, efforts in Colombia and Venezuela appear hopeful.

What Foreign Private Investors Can Do

Foreign manufacturers are a direct channel for the transfer of production, managerial, and marketing techniques. Foreign banks play a significant role in financing the growth of local enterprise. Foreign enterprises increasingly should be mindful of the many ways by which they can improve their contribution to local social welfare as well as to economic life.

The joint equity venture offers promise in this respect. Combining domestic and foreign capital, joint ventures are found in larger numbers in Latin America than anywhere else in the world. However, they are not a panacea since at times other ownership forms are more appropriate, even inescapable.

In the field of banking, the relatively new form of private development bank known as the financiera has been successful. It involves both equity investment and medium- and long-term loans. Effective operation of private financieras in Latin America dates back to 1941 in Mexico, 1959 in Colombia, and -- as a predominantly industrial investment entity -- 1961 in Venezuela. French and Spanish banks acquired minority equity shares at the outset of Mexico's first private financiera. U.S. banks began to purchase shares in Latin American financieras in 1959. There is need for additional foreign capital in creating and expanding financieras.

Latin America is short of credit in many other forms, notably export and import financing. The U.S. Export-Import Bank and Foreign Credit Insurance Association, as well as other foreign lending

institutions, could make an important contribution by liberalizing and expanding this form of credit. The inflationary situation in Brazil requires special procedures for loans in that country.

Other measures which foreign private investors can consider include: the establishment of an "industrial peace corps"; the formation of bi-national committees to bring together local and foreign private capital; and the launching of a research institute to promote private enterprise and private participation in development planning in Latin America. Foreign firms which are active in more than one country in the area can also make a particular contribution toward regional integration.

What Foreign Governments and International Agencies Can Do

The success of policies and programs of the U.S. Government, other governments, and international aid agencies that would give promise of materially strengthening the growth of Latin American private enterprise depends primarily on: 1) the amount and type of aid provided; 2) a co-operative attitude on the part of Latin American governments; and 3) the capacity to utilize assistance effectively.

The amount of resources from outside public sources is clearly important to the fulfillment of the objectives of the Alliance; yet by setting a higher priority on productive enterprise through replacing certain existing programs, foreign assistance programs can accelerate growth in ways that could lead to more vigorous and responsible local private investment.

Aid programs need also to be designed with closer attention to the absorptive capacity of recipient nations. While the Inter-American Development Bank has estimated that Latin American requirements for external resources amount to at least $23 billion over the next 10 years, the availability of skilled manpower is a critical bottleneck. Assistance to education should be designed to: 1) encourage adoption of programs of instruction which stimulate a recognition that worthwhile accomplishments can be made by individuals at all social and economic levels; 2) make room for the training of entrepreneurially promising employees in factories and business offices abroad; 3) improve research and training in economics in order to promote understanding of the forces engendering economic growth; 4) help ascertain future requirements for skilled and unskilled industrial manpower; 5) use incentives to encourage students to concentrate on technical and scientific studies; 6) promote applied research programs promising direct benefits to the industrial sector.

Worthwhile existing programs -- the support of productivity centers and technical consultants to industry, loans to development banks and corporations for relending to private enterprises, advice and assistance

in keeping inflation in bounds and in resolving serious balance-of-payments problems -- should be continued.

Aid programs outside the field of human resource development could also be revised to be more helpful to private enterprise. For example, roads are preferable to railroads in that they are generally a more efficient and rapid means of transport in Latin America, and offer opportunities for the development of trucking and for thousands of small entrepreneurs to run filling stations, garages, and construction firms.

Standardization and reliable continuous supply of industrial raw materials will become a reality sooner if greater external aid is earmarked for improving the extraction, grading, and transport of mineral resources and other materials, components and operating supplies. Plans for developing electric power might also be more helpful to private enterprise if they were more decentralized. The prevailing shortage of power, together with its concentration in a few areas, operates in favor of state industries which receive priority in power allocations.

Projects for regional development, including the support of industries serving regional markets and the fostering of preferential tariff and payments mechanisms, are ways of furthering regional integration, which should be promoted with the cooperation of private enterprise.

CATALOG OF INVESTMENT OPPORTUNITIES
IN LESS DEVELOPED COUNTRIES

The Office of Development Finance and Private Enterprise of the U.S. Agency for International Development has sponsored the preparation of a catalog of investment opportunities in the less developed countries based upon more than 1,400 feasibility and other studies made since January 1960 by private, governmental and international agencies both in the United States and abroad. The initial catalog was prepared under an AID contract by Checchi and Company, a private consulting firm in Washington, D.C. It will periodically be brought up to date by AID and the Office of Technical Services of the U.S. Department of Commerce as additional studies of investment opportunities in the less developed countries become available.

The catalog consists of three parts, containing progressively more detailed data and analyses. The first part is the Index to the catalog which lists investment opportunities by field of activity and by country, and contains the reference information required for using the other two parts of the catalog. The second part is a set of Keysort cards presenting abstracts of the data and conclusions contained in each of the detailed studies. These abstract cards are coded and punched to enable the user to obtain speedily the cards relevant to his interest. Cards can be selected from the complete set in a variety of ways -- by region, by country, by field of activity, by size of investment required, etc. The third part consists of microfilm copies of the detailed studies themselves.

The primary purpose of the catalog is to assist and encourage private investors in the United States and other countries to invest in productive activities

in the less developed countries. Accordingly, Indexes and complete sets of the abstract cards are available for consultation by prospective investors at the Office of Development Finance and Private Enterprise, AID, and the Office of International Investment, U.S. Department of Commerce, in Washington; at 40 field offices of the Department of Commerce in the United States; at the United Nations Headquarters in New York; and at the Organization for Economic Cooperation and Development in Paris.

In addition, each AID Mission has a supply of Indexes for free distribution, and a set of abstract cards relating both to the country and to the geographical region in which the Mission is located. Abstract cards dealing with Latin American investment possibilities are available in either Spanish or Portuguese, as well as in English.

A prospective investor wishing to obtain information on investment opportunities can quickly select the pertinent abstract cards dealing with the specific industries and size of investment of interest to him. If he finds an investment possibility on which he would like to have more detailed information, he can obtain a Xerox copy of the basic study reproduced from the microfilm at cost of reproduction. (The Index lists the cost of each study.) He can also purchase one or more of the abstract cards at a cost of US$0.35 per card.

The more than 1,400 studies summarized in the abstract cards are of three types -- detailed feasilibity studies of a specific investment possibility (e.g., a factory to manufacture transistor radios in Taiwan); broader, less detailed studies of the possibilities in an industry (e.g., the development of a refractories industry in Greece); and more general background studies containing information on the investment climate, taxation, government regulations, and other data of interest to prospective investors in a particular country. The fields of activity covered are manufacturing and processing industries, distribution and marketing, and service trades. These are classified by the Standard Industry Classification (SIC) system of the U.S. Department of Commerce.

A sample abstract card appears on the next page.

NIGERIA	Clay Products	3251	$542,000	$459,000	Type I	3/22/00267
COUNTRY	INDUSTRY	SIC	TOTAL CAPITAL REQUIRED (U.S. DOLLAR EQUIVALENT)	PROJECTED ANNUAL SALES (U.S. DOLLAR EQUIVALENT)	CLASSIFICATION	CODE

TITLE TECHNICAL AND ECONOMIC FEASIBILITY OF A STRUCTURAL CLAY TILE PLANT FOR WESTERN NIGERIA

ABSTRACT

MARKET: Presently no hollow clay tile demand since none manufactured. Would compete with generally used cement sand blocks which are often made on building site. Tile lighter and offers labor and space economies. Construction activities at ever increasing levels. Sales figure of $459,000 is net after delivery allowance.

PRODUCTION: Raw material from four sources tested. Determined that a combination of 75% Papa Alanto (sand free) and 25% Iju Clay would give best results. Five steps in raw material preparation and manufacture discussed. Plant capacity of 33,000 tons finished products annually. Fuel oil consumption could be largest variable factor from 4 to 15 tons per 100 tons clay, dependent on clay, kiln, etc.

FINANCE: Two Nigerians, Mr. Fani-Kayode and Mr. Faraz, said they would provide $50,000. Source of balance of funds not specifically discussed. Capital requirement $542,000 exclusive of clay deposits.

PROFITABILITY: 19% after taxes. If certified as Pioneer Industry and receives relief from income tax for 5 years, etc., return on capital as high as 32%. Income tax calculated at 8 shillings per pound (40%) in plant profit and loss statement.

MANPOWER: 90 unskilled, 25 semiskilled, 5 skilled (mechanics and shovel operators). Not discussed further.

LOCATION: At Papa Alanto, one mile from clay deposit; 20 miles from Iju clay deposit, and 35 miles from Lagos (finished product market). Water and utilities available.

INVESTMENT CLIMATE: Nigerian Government encourages private enterprise. Financial participation not discussed specifically. Constitutional guarantees against expropriation and nationalization without compensation. Profit and capital may be freely withdrawn by nonresidents and at will.

CONCLUSION: "The initiation and success of the envisioned tile scheme would be contingent upon the availability of substantial outside financial participation and upon the active participation of a technical partner who has background in an operation of this type."

SPONSOR'S REPORT OF CURRENT STATUS: "Successfully implemented. In production."

Eldon P. Farly and S. A. Cogswell, Standard Research Institute
AUTHOR

Rockefeller Brothers Fund
SPONSOR (S)

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COMMENT ON INVESTMENT OPPORTUNITY:

This report covers an opportunity for structural tile production in the Lagos area of which advantage has already been taken by interested investors. A similar possibility might exist in the area of the still larger but less modern city of Ibadan. If structural tile proves popular at Lagos, its introduction at Ibadan would be logical. The present study, however, reviewed clay deposits only in the vicinity of Lagos. US Agency for International Development guaranties would be available for investments in Nigeria.

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HUMAN RESOURCES DEVELOPMENT

EDUCATION, MANPOWER AND ECONOMIC GROWTH:
STRATEGIES OF HUMAN RESOURCE DEVELOPMENT

Frederick Harbison and Charles A. Myers

[New York, Toronto, London, McGraw-Hill Book Company, 1964, xiii and 229 pp. US$7.50.]

A summary of the main points in the book begins on the next page.

[This book is a project of the Inter-University Study of Labor Problems in Economic Development, which is a joint research and educational enterprise of staff members from the University of California (Berkeley), Harvard University, Princeton University, and Massachusetts Institute of Technology, in association with colleagues in other institutions in the United States and abroad. Since its inception in 1954, this extensive program has been directed by Clark Kerr, President of the University of California, Professor John Dunlop of Harvard, Professor Frederick Harbison of Princeton, and Professor Charles Myers of M.I.T. As stated by the four directors in the Appendix to their book, Industrialism and Industrial Man (Harvard University Press, 1960):

> "The objective of the Inter-University Study is to promote and sponsor comparative studies of the role of human agents in the processes of economic development. The purpose is both to

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Charles A. Myers is Professor of Industrial Relations, Massachusetts Institute of Technology, Cambridge.

conduct research and to help to develop people in different countries as experts in the analysis of industrial relations and manpower development problems. The Inter-University Study has been interested in the past and will be concerned in the future with both research and operations, with fundamental knowledge and policy applications."

Grants from the Ford Foundation and Carnegie Corporation of New York, as well as help from countries in which studies have been made have provided the financial support for the program.

Education, Manpower and Economic Development is the most recently published book sponsored under the program. It is based on Professors Harbison and Myers' many years of study, travel, consultation, and experience with problems of human resource development in numerous countries. The authors have also drawn on unpublished manpower and education surveys to which they had access because of their work with various international agencies, as well as on ten essays, to appear shortly in a book of country studies, which they are currently editing as a companion volume.

The following summary is reprinted from the Carnegie Corporation of New York Quarterly, Vol. XII, No. 2, April 1964.]

The economic return from a capital outlay for a dam can be measured fairly easily -- in kilowatt hours of electricity, in acres of land under irrigation. The return on a comparable investment in education cannot be calculated so precisely. Yet no economist (or anyone else who has given any thought to the matter) doubts that trained manpower is the sine qua non for economic development; without it, the other necessary elements such as capital, natural resources, and trade cannot be exploited.

Thus any nation, rich or poor, makes two major kinds of investment to promote its well-being and growth. It invests in things and in people. What the proper balance is between these two kinds of investment and, just as significant, what priorities should be established within each kind, are important questions for all nations, but particularly for the scores of economically underdeveloped countries now pressing for a rapid rise in their standards of living.

These questions, and numerous related ones, are the subject of Frederick Harbison and Charles A. Myers' recently published book. Its

subtitle, "Strategies of Human Resource Development," states its theme. It is unfortunate that human beings must be referred to as "human resources," as if they were so many mineral deposits or forests. Though the authors do use the phrase, they do not have a restricted, "economic" view of man, or of economic development, for that matter. At the outset they say: "As economists, we are first of all interested in economic growth. But as peripatetic observers of many societies, we are convinced that the world-wide aspiration for development is a quest as well for status, prestige, recognition, and social and political modernization." A basic assumption of the book is that the political and social objectives cannot be divorced from the economic growth objectives of the modernizing nations; the point is that the development of human resources is the key to modernization of <u>any</u> sort. "If a country is unable to develop its human resources, it cannot develop much else, whether it be a modern political and social structure, a sense of national unity, or high standards of material welfare."

Education

When we think of how to develop human resources, most of us (not only laymen, but economic planners as well) tend to think in terms solely of the formal educational system: build the schools; staff them somehow; provide means for an adequate number of students to get to and through them.

It is not so simple, of course. There is the matter of financing, for one thing. And although most countries probably invest too little in formal education, some apparently invest too much, or invest in the wrong kinds. Both India and Egypt, for example, produce more university graduates than their economies can employ. Almost all of the underdeveloped countries are trying to provide primary education for all their children -- with very few secondary schools for them to move on to. Thus, they will add to the already sizeable surpluses of ill-equipped, but highly aspiring, personnel for a labor market unable to use them productively.

Clearly, formal educational systems must be rationally planned; limited resources must be allocated to produce a balance appropriate to the needs of the particular country. But this is only part of the story. Harbison and Myers' major thesis is that a strategy of human resource development has <u>three</u> major components, of which formal education is only one. Simultaneous and equal attention must be paid to the two others: the building of incentives and the utilization of possibilities for on-the-job training.

Motivation and Incentives

No educational system can produce the required personnel for critical occupations if the requisite number of people is not motivated

to enter them. If the pay-off in both prestige and money is greater for lawyers, for example, than for agricultural specialists (as is true in many underdeveloped countries), the mere existence of a good agricultural school will not suffice. Necessary incentives must be built deliberately and on the basis of the country's needs, not, as is so often the case, on mere level of educational attainment or degrees, or family status, or political connection. In some countries, say the authors, it might be necessary to provide engineering technicians, for example, approximately the same rewards as full-fledged engineers; it might be desirable to give equal pay to a doctor who insists on practicing in a city and a medical technician who is willing to work in a rural area. And in the most underdeveloped countries, the incentives might need to be very strong indeed; with fantastic shortages of both money and personnel, these countries must make sharp choices about whom to educate and in what fields, and some may need to impose a period of national service on those thus educated.

Training

The burden of most training, as distinct from education, should rest on employing organizations and agencies, governmental and private. This makes it possible for the formal educational system to be run more cheaply; it is also more efficient.

"Human capital formation may start with formal education," write Harbison and Myers, "but it does not end there. Most managerial, technical, and craft skills, for example, are developed on the job much more effectively than in vocational schools. Indeed, in many countries vocational or trade schools are quite inefficient and wasteful instruments of human capital formation." The authors claim that the rich potentialities of in-service training have not begun to be developed on any scale in most of the modernizing countries, whether by government (often the largest employer) or private businesses or foreign technical and economic assistance missions.

Strategies of Development

These three components -- formal education, incentives, in-service training -- should comprise the overall strategy of human resource development for countries at all stages of development, from primitive to modern. But the priorities that should be established, particularly in the formal educational system, would vary for countries at different stages. A large portion of the book is devoted to policies that might be pursued by countries at different levels of human resource development: underdeveloped, partially developed, semiadvanced, and advanced. Harbison and Myers group 75 countries into these four levels, on the basis of their enrollments in secondary and higher education proportional to the relevant age groups in the population. Not surprisingly,

there is a very high positive correlation between a nation's gross national product per capita and its level of human resources development as measured in this way.

The authors develop a suggested strategy for countries at each of the levels, taking into account political and social forces and needs as well as economic ones. For the underdeveloped countries, the dominant political imperative is "localization," that is, the replacement of foreigners by nationals in key public and private posts. The basic economic necessity is to increase the productivity of agriculture and raw materials. A major social objective is the expansion of primary education.

The logical strategy, therefore, calls for a crash program to increase the output of secondary education in order that localization may be brought about. University graduates are needed also, and must be educated abroad until the country can develop its own institutions of higher learning. At the primary level, the best way to increase enrollments would be to curtail dropouts rather than to increase the intake of students in the first years; in other words, admit fewer but keep them in school longer. Finally, heavy reliance for vocational training must be put on employing institutions.

In the partially developed countries, the economic need is to build a base for industrialization while expanding agricultural production. There are acute shortages of all categories of professional and technical personnel. Universal primary education is attainable. Increasing populations and underemployment and unemployment create strong pressure for rapid growth and reform.

At this level, Harbison and Myers give top priority to the reform and expansion of secondary education. Next, the education of subprofessional personnel and technicians must be expanded. In higher education, more emphasis should be placed on high quality education in science and engineering. The cost of primary education must be kept as low as possible, and the quality as high as possible, through the use of new technologies whereby relatively unqualified teachers may be used effectively. And, it is necessary to increase the relative pay of engineers, teachers, and technicians in order to lure students into those fields.

In the semiadvanced countries, the major economic objective is rapid and massive industrial development. There is increasing clamor for more education at all levels, as compulsory primary education increases the demand for secondary education which in turn raises the number qualified for university. Here the key element in the strategy calls for the reorientation and reform of higher education, with more emphasis on scientific and technical education along with improvement

in instruction in other fields. The quality of secondary education must be maintained despite increasing enrollments; this means using better methods of teaching and better teachers.

In the advanced countries, the authors state, "The new imperative is innovation, not only in science and technology but in the area of human organization as well." Higher education, particularly at the post-graduate level, becomes the top priority. With mass primary education long a reality and universal secondary education virtually one, emphasis should be placed on improving the quality of secondary education, and on expanding higher education through junior colleges, higher technical institutions, and universities. Even the advanced countries must expect to make greater proportional investments in developing manpower, "for the future of those countries depends more upon the development of brainpower than upon the development of physical resources."

Planning

Such a three-pronged strategy (formal education, incentives, training) obviously requires coherent planning. For each country, it is necessary to make "a systematic assessment of its human resource problems and requirements. Such an assessment is much more comprehensive than a manpower survey or a study of formal education. It should include, at the minimum, an analysis of the following: 1) manpower requirements; 2) the system of formal education; 3) institutions for in-service training and adult education; and 4) the structure of incentives and the utilization of high level manpower."

When such an assessment has been made, targets can be set, and the manpower development plan integrated with the overall development plan for economic development. Harbison and Myers devote several chapters to discussing how this can be done.

"This book was deliberately designed as a blueprint for action rather than solely as a scholarly academic exercise," the authors write. It is thus of important interest to all concerned with development planning. And although it must be followed with close attention because of the number of important ideas advanced, it can also be read with profit and interest by non-economists.

THE ROLE OF INCENTIVES
IN HUMAN RESOURCE PLANNING

S. C. Kelley

[From Planning Education for Economic and Social Development, edited by Herbert S. Parnes, the Mediterranean Regional Project; Paris, Organisation for Economic Co-operation and Development, 1964, pp. 27-37, free.]

[In their book, Education, Manpower and Economic Growth (see pages 111-116 above), Professors Harbison and Myers point out that an essential aspect of human resource development is a strengthening of incentives for people in developing countries to commit themselves to the types of work which are required for accelerated economic and social development, and to obtain the education and training necessary for such activities. The lecture excerpted below deals with the nature of this problem and some of the ways in which it could be alleviated.

Excerpts from the lecture begin on the next page.

Planning Education for Economic and Social Development contains the lectures presented by various experts at a training course in human resource development conducted by the OECD under its Mediterranean Regional Project. The five papers in Part I deal with the problems and methods of measuring and explaining the relationships between education and economic growth. Part II contains nine more technical papers on the methodology and limitations of the manpower requirements approach to educational planning. In Part III seven papers discuss the pros and cons of various methods of formulating

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and costing educational targets. An appendix contains two proposals for research into the economics of teaching methods and the qualitative aspects of educational planning.]

The development of educational facilities and teaching resources is a means of effecting necessary changes in manpower characteristics. It is obvious, however, that the development of educational facilities and opportunities is not meaningful in the absence of the motivation to use them and to use them in appropriate ways. Further, many of the changes required by economic development are changes in the ways in which labour resources are used, rather than in the qualitative characteristics of the resource. In both instances, the system of rewards or penalties which induce "appropriate" behaviour, is a major factor. It assumes particular importance where the required changes are of great magnitude and where resistance to change is great.

The developing countries with which we are primarily concerned are those with some elements of an industrial order. They anticipate a rapid and extensive development in the direction of industrial expansion, but a very large part of the existing economic structure is characterized and bound by the traditional forms of an agrarian society. In this situation, our concern with motivation and incentive is a concern for the complex of human attitudes and motivation which result in specific acts of commitment to a work role and a way of life. Whether these acts will provide, in the aggregate, the social arrangement necessary to industrial efficiency depends ultimately on the way each individual perceives the hazards and the opportunities involved in the process of change.

It is implicit, in the value assumptions which lead to economic planning, that the benefits of an industrial order will exceed the costs. Yet the process contains no guarantees that the benefits will accrue to those who bear these costs. Benefits are received and costs are paid by individuals. Thus, no aggregate balance of costs and benefits is meaningful except, perhaps, in the long term.

Nations and other social institutions may be committed to the long term; individuals rarely are. Although we assume that the developing countries are committed to industrialization, it is probable that the nature of this commitment and its implications are evident only to a very small number. Many others may aspire, as individuals, to a higher standard of living without understanding, in any clear way, the personal implications of getting it.

The efficiency of an industrial society rests, ultimately, in the specialization of human tasks and the mobility of human resources. It is the role of the system of incentives to develop individual commitments to mobility or, in other terms, to appropriate labour market

behaviour. A labour market is the institutionalized form of a set of human attitudes and human values. A commitment to a labour market is a commitment to change in work roles and way of life in some relation to an established system of rewards. The first requisite of an industrial order is the formation of this commitment. Its formation takes place in conflict with traditional values and traditional institutions. How difficult the task of formation may be will depend on the strength of the traditional restraints and the efficiency and adequacy of the new system of rewards.

Motivation and Mobility

In looking, then, at the problems of motivation in the context of developing economies, or at the policies appropriate to these problems, the differences among them are likely to be differences of magnitude, rather than of kind. All such policies are directed towards maximizing individual rewards, minimizing individual costs and communicating the nature of alternative choices. In the classical view of incentives and motivation, primary importance is attached to the maximization of rewards in relation to rather marginal and precise changes in resource allocation. In the real situations which are characteristic of the developing countries, it seems much more likely that the most effective policies will be those designed to mitigate the social cost of change and to communicate the alternatives of choice.

In a most general sense, there are three types of motivational problems falling within the scope of this discussion. At the most basic level there is the problem of labour force commitment, or, more explicitly, the problem of inducing movement between contrasting and conflicting social milieux. Here, we are concerned with evaluating the impact of the restraints imposed on industrialization by the existence of a traditional order whose institutions and values are in conflict with required individual roles in an industrial society. Further, we are concerned with the policies appropriate to the reduction of these restraints and the validity of any assumptions concerning their feasibility that may be implicit in manpower projections.

At a second level is the need to induce massive and basic movement within the industrial structure, both directly and indirectly through the system of education. These are movements involving individuals who are already committed to work roles in an industrial society but whose current roles are inconsistent with the best use of their potential capacities. It is at this problem level that we are concerned with policies designed to influence the occupational implications of the flow of students through an educational system, and changes in the characteristics of the existing labour force through retraining or other devices.

A third level includes those problems imposed by the need for factor mobility and structural flexibility in a dynamic industrial economy. Here, the system of incentives is oriented toward the inducement of

individual response to changes in the demand for labour arising from the impact of new technology, changes in the relative scarcity of resources and shifts in patterns of consumption.

The distinction between this problem category and the preceding one may appear ambiguous or even spurious, since they are of the same general order. However, in developing economies, they are of quite different magnitude and may require rather different assumptions concerning appropriate policies and the implication of these policies for economic projections. This difference is of particular relevance in view of the fact that market economies have relied on the wage structure and the incidence of unemployment to effect "appropriate" labour market behaviour. It seems evident that wage differentials cannot accomplish, in the short term, changes of the magnitude required by the process of industrialization as distinguished from those involved in adjustments within an already industrialized economy. Furthermore, in the latter, unemployment, as an incentive to change, is increasingly limited to very short-term frictional problems by the growth of security objectives and their institutionalization in public systems of compensation and trade union practice.

Labour Force Commitment

The process of labour force commitment involves individual acceptance of the discipline of an industrial work role and a self-directed rather than group-directed way of life. In his insightful study of the development of an industrial society in 19th century America, Alexis de Tocqueville describes this process as the growing "tendency for the individual to draw apart from society and to rely on his own hands for his own destiny." It is this attitudinal change that is the process of labour force commitment and the requisite of an industrial order.

The economies and cultures of the developing countries are rooted in family enterprise. The known ways of life and work are centered in the family unit. The determination of individual roles and the rewards of these roles, including status, security and self-image or self-esteem, is made here. The system of rewards in a primary group gives emphasis to status and status-oriented roles. The interaction within such groups develops strong loyalty to the dependence on the group for all forms of security and self-concept. The primary problem of labour force commitment is to break the ties of the traditional group by a system of rewards that will overcome the restraints of group loyalty and substitute for the rewards of status and self-esteem that it offered.

In tradition-oriented groups, the amount of interaction between groups is likely to be minimized and the individual values, concepts and perceptions are group-derived. Education and experience, as a means for the communication of alternative ways of life, occur within the narrow confines of primary group associations and are more likely to limit than enlarge the individual perceptions. Those who are most ready to break

the ties of the primary group are the dissidents. At the same time, they are those who are least likely to develop the kind of commitment to labour force behaviour that is essential to economic efficiency.

The magnitude of the problem of commitment in developing countries is not easily estimated. One economist (Clark Kerr) believes that the force of the process of industrialization is so strong that it will sweep the earlier behavioural patterns before it. In his view, the break with the past and the development of a new commitment to an industrial order will not be difficult. Another (Mehuis M. Turin) suggests, in contrast, that "it is possible for a group of persons to be ready to change from certain status and role arrangements, without being ready to adopt and commit themselves to any other particular set of arrangements" and that "the way of work and the rewards of work in traditional societies are most frequently central to their way of life." Without elaborating on this disagreement one might suggest that although the process of industrialization, once under way, may be irresistible, it does not follow that the processes by which it works out are without great cost and great resistance, in particular where industrialization occurs at accelerated rates, as it is currently in the developing countries.

It is more descriptive of the present situation to say that there is, in being, a major and widespread change in economic aspiration toward the standard of living but not necessarily toward the ways of life and work that are associated with an industrial society. It seems evident that the process of change will require a much greater concern with the means of commitment than was evident in the evolution of the developed countries. The economic institutions of the latter, including the system of economic rewards, developed over the long term. They were derived from specific acts of innovation and invention, in cumulative fashion. They were not a function of clearly defined aspiration, but were induced in conjunction with aspirations and acts of commitment. This concurrence of aspiration and commitment permitted a pragmatic and relatively easy evolution of the general society toward new forms and new directions. In the United States, for example, they developed in a culture with few traditional restraints and a strong commitment to change.

In contrast, the developing countries possess highly traditional cultures and their commitment to change is highly generalized. Their current aspiration toward industrial development is derived from extended contact with the developed countries. The specific forms of aspiration are derived from existing situations, from the known rather than the unknown. Thus, they are not acquired incrementally, but in full form while, at the same time, the means of achievement are rudimentary. The rapidity and magnitude of the changes inherent in industrialization will require, in these situations, a radical break with the past.

It is doubtful whether, in any absolute sense, the developed countries reflect a sequence of events that must be or will be matched by the

developing nations. It may well be possible, as some analysts believe and as some countries are currently attempting, to minimize the impact of change by planned compromise between traditional and industrial practices. However, it is obvious that the process of industrialization does carry with it certain forms and commitments which will change developing nations in similar ways. One must doubt that it is possible to reconcile, in significant degree, the rewards of craftsmanship with specialization of task, the independence of the proprietorial form with the interdependence of a rationalized industry, or the harmony of an agrarian society with the conflicts of interest in an industrial order. If the rate of industrial development is as rapid or the time for change as brief as that assumed in the developing countries, the problems of commitment seem certain to be limiting and the need for assessment real.

We may also note that the problem of commitment is most difficult in a free society where individual choices are given paramount importance and where social decisions and social actions must reflect the sum of individual values. In an authoritarian society, the factors or means which induce appropriate economic behaviour in voluntary ways may be important. In a democratic context, they are critical.

In assessing the validity of economic projections and the possibility of modifying the resource base on which they rest, it is therefore essential to define and evaluate the factors which affect the relevant behavioural norms. An adequate plan for economic development must include an assessment of the various means required to induce the kinds of labour force commitment and labour market behaviour which are implied in the resource projection.

Status and Security Incentives

The inducements to labour force commitment are both positive and negative. They include, on the one hand, the various means by which the individual cost of commitment is alleviated and, on the other, the development of positive incentives to change. The major restraint imposed by the kinship relation is the loss of security and individual status which are derived from the primary group association. At the same time, problems of insecurity and the absence of work-derived status are characteristic of industrial roles.

It has been typical of most developing economies that individuals compromise the transition by forming limited or partial commitments, moving back and forth between the kinship association and the industrial role. This partial commitment is limiting on the development of an experienced and efficient labour force and thus on the rate of industrial development. Consequently, policies to facilitate the development of commitment should include the means to develop new primary group associations within the industrial community and group roles that can substitute for those of the traditional kinship type.

In this respect, it is recognized that the development of job-oriented trade unions has served this purpose in many developed countries. They have established some form of status structure within the work situation and provided opportunities for status achievement within the organization. Further, they have usually contributed to the degree of job security attained by the individual, in particular in terms of restraints on arbitrary actions of the employer. Recognizing that in the developing countries trade unions are likely to be politically oriented rather than job oriented, it would seem to be appropriate public policy to promote and encourage the development of job-conscious unions and collective-bargaining processes similar to those of the economically advanced countries.

The developing countries are, almost universally, limited by the existence of a large corps of unskilled unemployed in the industrial sectors. In large part, this condition is a result of the fact that the transition from a traditional to an industrial work role requires a level of skill and training unavailable in the traditional society. Policies which are expected to increase mobility and encourage labour force commitment should facilitate this transition by the extensive development of vocational training facilities in the areas from which movement occurs. In other terms, it would be desirable to move individuals from traditional to industrial work roles indirectly through a training process which could be structured in relation to industrial needs, rather than to rely on the uncertain forces of an undeveloped market mechanism for this purpose.

A third area in which public policy may be directed toward the reduction of mobility restraints in the process of labour force commitments stems from the relation of urbanization to industrial growth. Historically, rapid urbanization has been disruptive of traditional social values and in particular of the family relationship. The problem of assimilating migrants into urban life is obviously difficult, yet it seems possible to alleviate it by the development of low-cost housing, the creation of community organizations to plan and administer the integration process, as well as other means to establish a new community relationship. In brief, we are suggesting that in social change, as well as in medical practice, preventive practices may be less costly than curative procedures.

Education as Incentive

Finally, we would suggest that an important area of action in offsetting the restraints of the traditional order is in the process of communicating alternative choices. In the long term, a primary instrument for this purpose is the extension of compulsory education. Education should change the level of aspiration for many and should provide new concepts of status within the structure for others. Educational planning should recognize the implications of education in this respect and the patterns of education should develop in ways that are consistent with these needs.

This does not imply that education should be directed toward the acquisition of vocational skills or that it should "direct" young people in particular vocational directions. Rather, it suggests that education should have its focus in the present and future. It should create individual sensitivity to the challenges beyond the world of tradition and extend the range of perceived opportunities.

It is apparent that education has not performed this role in the past and probably is not doing so to-day. The structural relationship between educational attainment and occupation in developing countries suggests that education, and in particular higher education, has been tradition-oriented. It had developed human resources on the basis of traditional status considerations in ways that are inconsistent with the realities of an industrial society. The result is a waste of educational resources. More important, it has limited the intellectual lives of its constituents by leaving them in work roles that do not utilize their intellectual capacity.

Over the long term, education may be a primary instrument for commitment, but in the immediate future other means of communicating alternatives may be equally important. One possibility is the extensive development of a system of vocational guidance and counselling. It is implicit in our assumption of labour market allocation that individuals will respond in the "right" ways and that the total of individual movements will correspond with the structure of labour demand. Yet, apart from the many other restraints, mobility is restricted simply because the individual rarely knows the rules of the game or his position in it.

A recent study of the long-term unemployed in a developed country suggests that a primary barrier to occupational movement is a lack of knowledge concerning their future in their primary occupation and the alternatives available to them. A very large proportion of these workers had the intellectual capacity for retraining to higher occupational levels, including those in very short supply, such as technical and semi-professional occupations. While some were bound to their present status by other ties, the majority were limited by an inability to assess the available opportunities in relation to their present status. They were uninformed concerning their own potential to perform in occupational roles other than those in which they were experienced. They conceived of the range of opportunity in terms of their experience and their aspirations were generally much higher than their self-concept of capacity. They had a limited knowledge of the economic factors affecting their current status, including shifts in the industrial structure and the potential labour requirements of the firm or industry to which they were attached.

We may note, parenthetically, that economists have not yet developed a workable methodology for distinguishing the effects of short-term forces from those of long-term trends, at least in the real world. Yet, it is implicit in the mobility assumptions commonly applied, that the individual

worker is expected to make this analysis on intuitive grounds and respond "rationally" to the situation in which he finds himself. We are, in short, expecting a "rational" man to gamble his present status and security, however little, against a future of unknown value in a game where the probabilities of success are unknown.

Much of what is suggested here in relation to the problem of labour force commitment is equally relevant to the problem of inducing appropriate labour force behaviour. Given the acceptance of an industrial work role and an industrial way of life, it is essential to the process of economic development that individuals react appropriately to changes in the structure of manpower requirements.

Wage Incentives and Labour Mobility

In the developing countries, appropriate behaviour requires the motivation for many to continue formal education to higher levels and to choose as career objectives occupations of a professional, technical or management nature. For others, it involves the desire to raise their occupational level through acts of vocational training or retraining. In the broadest terms, it involves for all the motivation to change work situations in response to opportunities for maximizing individual satisfactions.

In these countries, mobility is restricted and the patterns of movement distorted by the fact that money wages have not acquired the necessary importance in the hierarchy of rewards relative to the traditional rewards of status and security. This condition is reflected in the extent to which the output of institutions of higher learning is determined by traditional status considerations rather than by the reflection of productivity in wage and salary levels.

The development of appropriate labour market behaviour thus involves policies and programmes which modify the existing status structure and develop new status symbols. These may take the form of honorific recognition or social prerogatives but, in the long term, they are more likely to be effective in material forms. The current explosive concern for economic development is a reflection of a new and general acquisitive bent in the developing countries. It is, in large degree, the material standards of the developed countries which provide the impetus for change.

Given this generally higher level of economic aspiration, the wage structure and the magnitude of wage differentials are increasingly relevant to the occupational distribution of the current labour force and to the flow of entrants through the educational systems into the labour force. Rising wage levels are likely to induce an increase in motivation toward the acquisition of material rewards. Wage differentials are, in themselves, a reflection of a new status system. There is significant

evidence in the developed countries to suggest that wage rates are viewed by workers in relative, more than in absolute, form and that wage differentials are more effective as motivations to movement than are changes in absolute monetary rewards.

The development of a skilled labour force will require a maximum upgrading of those now in unskilled occupations and a monumental increase in the proportion of students continuing through upper-secondary and higher levels of education. Neither of these requirements can be met in the absence of adequate differentials in the earnings level of skilled and technical occupations as contrasted with unskilled employment. Moreover, the problem of the unskilled unemployed is certain to be a difficult and continuing one in developing economies, and policies which minimize differentials can only prolong and intensify it.

Beyond the occupational pull of differentiated earnings, it seems essential for developing countries to provide other monetary incentives to occupational movement. Several countries with tight industrial labour markets now provide various forms of subsidies to encourage and facilitate appropriate movement. These include transportation allowances, cost-of-living differentials, and subsistence allowances while moving toward or retraining for new occupations. An extension of these forms of incentive would be justified by the manpower needs of developing countries. Further, it could be appropriate and effective to subsidize students or, in essence, to pay them for continuing education, perhaps with differential allowances for specialization in particularly scarce occupations. In essence, policies of this type could extend the democratization of education and, in doing so, reduce the existing restraints imposed by a tradition-directed system of higher education.

Conclusions

In this brief discussion, we have touched on a few of the many aspects of the relation between motivation, incentives and manpower requirements in developing economies. We have suggested that it is unrealistic to assume that major realisation of labour resources will occur without attention to and change in the various systems and forms of incentives. The magnitude of these changes is great and the policies relevant to them are varied. It is neither reasonable nor consistent with the intent of planning to draw heavily in this respect on the experience of developed countries, where economic evolution has frequently occurred at great individual cost. Factors of motivation and incentive are as relevant to manpower projection and educational planning as the more tangible factors of resources. If they are not by nature measurable, they are, at least, susceptible to reasoned consideration in the development and evaluation of manpower and educational projections.

EDUCATION FOR A DEVELOPING REGION:
A STUDY IN EAST AFRICA

Guy Hunter

[Political and Economic Planning and the Institute of Race Relations; London, George Allen and Unwin Ltd., 1963, xvi and 119 pp.]

Based upon extensive field research in the East African countries, Guy Hunter describes the main characteristics of their educational system; analyzes in detail the nature of their present and prospective educational needs and problems; and assesses the extent to which their policies and programs are adequate to cope with existing and anticipated difficulties. He focuses particularly upon the types of magnitudes of assistance which these countries need and are likely to obtain from foreign governments and private institutions and from international agencies. While deeply sympathetic with African expectations, the author's conclusions and recommendations are based upon a realistic assessment of resource availabilities, both in East Africa and abroad. A particularly valuable aspect of Mr. Hunter's study is his knowledge of similar and contrasting problems in other developing countries.

This study, sponsored jointly by two British research institutions, Political and Economic Planning (P.E.P.) and the Institute of Race Relations, is the first part of a larger research project undertaken by P.E.P. with the aid of a grant from the Ford Foundation. The project deals with problems of educational development in Africa, focusing particularly on the adequacy of educational opportunities provided for African students in the United Kingdom and with possibilities for increasing the availability of British teachers for service in educational institutions overseas.

Guy Hunter of the Institute of Race Relations in London has had long experience in education and industrial training in Africa and Southeast Asia.

RESEARCH PROGRAM OF
THE AGENCY FOR INTERNATIONAL DEVELOPMENT

The U.S. Agency for International Development (AID) is sponsoring a research and analysis program on various aspects of the development process in less developed countries. As described in a recently published AID brochure, the purposes of this program are:

(a) to add systematically to knowledge about the forces and processes at work in the economic growth and social modernization of developing countries;

(b) to create and explore improved technical materials and methods for use by AID and other technical assistance agencies in the promotion of economic development; and

(c) to evolve and adapt scientific methods of analysis, using a quantitative approach wherever possible, for predicting and assessing the results of AID program actions and for the comparison of alternative actions.

Two further considerations of nearly equal importance guide AID in the conduct of this program. It should provide for the growth, in numbers as well as in breadth, of the community of creative researchers engaged in work and advanced training in relevant fields, and it should benefit the competence and orientation of research in developing countries.

Research under this program is undertaken by universities, independent research institutions, and private business firms, as well as by government agencies. At present, research projects are under way or contemplated in the following fields:

Agriculture -- soils, fertilizers, and irrigation; crop and livestock improvement and production; equipment, storage, and processing; institutions and services; economic studies.

Public Health -- nutrition; communicable disease control; manpower problems in public health; public health and economic development.

Human Resources -- design and structure of educational systems; psychological factors; curriculum content; teaching and training methods.

Material Resources -- natural resources; mechanisms of industrialization; transportation, communications, and power; adaptation and innovation engineering in industrial production.

Social Systems -- population dynamics; rural development; urbanization; leadership and political identification; institution-building.

Systems Analysis -- economic analysis; analytical aids in development decisions; strategic analyses; data needs and handling.

Operations Analysis -- policy and program coordination problems; country studies; analysis of foreign assistance modes and channels; pilot design and evaluation of projects; administrative analyses.

For additional information regarding this research program, write to the Science Director, Office of Technical Cooperation and Research, Agency for International Development, Washington, D.C. 20523.

SOME RECENT BOOKS

Powelson, John P., Latin America: Today's Economic and Social Revolution; New York, Toronto, London, McGraw-Hill Book Company, 1964, xi and 303 pp., US$9.00.

The title of this book is descriptive of its contents in a general sense but fails to indicate its unique character and value. It is not primarily a description or an analysis of "today's economic and social revolution in Latin America." Rather, its major purpose is to explain the differences and their significance in the attitudes and policies of Latin America, on the one hand, and of the United States, on the other, with respect to the economic issues and problems important for Latin American development and Latin American-United States relations. As such, it is addressed both to North and to South Americans. It can also be read with profit by anyone seeking to understand the relationships between the attitudes and institutions of a society and its development problems and policies.

Professor Powelson has taught economics for many years in Latin American and U.S. universities, and is currently Director of the Program on Integrated National Accounts, Centro de Estudios Monetarios Latinoamericanos, Mexico City. He is well acquainted with the intellectual characteristics and concerns of Latin American professionals and students. He understands the images, true and false, which they have of the United States, and of its policies toward Latin America. Conversely, he is familiar with the images, true and false, which North Americans have of the Latin American countries and their policies. Addressing each group in turn, he seeks with facts and analysis to give each a truer picture and a deeper understanding of the other's problems and purposes.

This "dialogue" is conducted within the context of the major economic problems and issues relevant to the changing conditions of Latin America today. Separate chapters deal with such subjects as private versus public enterprise in Latin American development, agrarian reform, monopoly and

competition, the dilemmas of raw material-producing economies, inflation, economic integration, development planning, and foreign aid. In each chapter, Professor Powelson explains the nature of the problems; analyzes the often divergent views and policies of the Latin American countries and of the United States; interprets the reasons for and significance of these differences in terms both of varying interests and of mutual misconceptions; and indicates the ways in which the correction of these misconceptions on both sides would enlarge the area of mutual understanding and agreement. These discussions are not abstract, but are empirically grounded in the relevant factual material and are illustrated by characteristic quotations from the writings and speeches of representative North and South Americans.

Schultz, Theodore W., Transforming Traditional Agriculture; New Haven and London, Yale University Press, 1964, xiv and 212 pp., US$6.00.

This book presents a new theory of the process by which traditional agriculture is transformed, and explains the operational implications of the theory for policies and programs designed to accelerate the modernization of agriculture in the less developed countries. It is the fruit of many years of research and thinking by Professor Theodore W. Schultz, one of the leading economists in the United States, who has had a special interest in the field of agriculture.

Professor Schultz sums up his main findings in the following paragraph:

> "The central argument of this study...runs as follows: The economic basis of the slow growth of a [poor agricultural community]...is not to be found generally in observable inefficiencies in the way the traditional agricultural factors of production are allocated; nor is it to be explained by sub-optimum rates of savings and investment in such traditional factors, because the rate of return at the margins is generally too low to warrant additional savings and investment, given anything like normal preferences and motives. The economic basis for rapid growth under these circumstances does not lie in exhortations pertaining to work and thrift. The key to growth is in acquiring and using effectively some modern -- i.e., nontraditional from the point of view of the experience of the people -- factors of production. These modern factors are often concealed by economists under an expository contrivance called technological change. The suppliers of modern agricultural factors are, among others, research people who work in agricultural experiment stations. Their contributions in this connection are of critical importance. Farmers in their role as demanders of the new factors accept them when they are truly profitable. But, typically, farmers in traditional agriculture do not search for them. In the end, much depends on farmers learning how to use modern agricultural factors effectively.

At this point, rapid sustained growth rests heavily on particular investments in farm people related to the new skills and new knowledge that farm people must acquire to succeed at the game of growth from agriculture."

In the process of working out this explanation and testing it against available data, Professor Schultz dissents from many generally held opinions about the causes and remedies of poverty and stagnation in traditional agricultural communities. On both theoretical and empirical grounds, he argues against such views as:

- that the returns are high on capital invested in the factors of production in traditional agriculture and hence that additional investment in these traditional factors would yield a high return;

- that a significant proportion of the labor engaged in traditional agriculture is underemployed and hence makes little or no contribution to production;

- that cultural factors account for the failure of many traditional agricultural communities to accept or initiate innovations;

- that raising the productivity of agriculture requires large-scale farming units;

- that economic development strategy should give priority to industrialization;

- that efficient decisions regarding production and innovation on individual farming units could be made by central government authorities despite their lack of knowledge of the specific situation of the farm, of the guidance in factor allocations provided by market indicators, and of the pressures and incentives provided by personal benefits and losses consequent on their decisions.

While a few of Professor Schultz's conclusions may be based on insufficient evidence (e.g., that cultural factors can be discounted in trying to transform traditional agriculture), this is one of the most important and useful books to be published on agricultural development.

Eicher, Carl K. and Lawrence W. Witt, editors, Agriculture in Economic Development; New York, Toronto, London, McGraw-Hill Book Company, 1964, vi and 415 pp., US$10.00.

This is a collection of readings on agriculture as a key sector in economic development. The 25 selections are reprints of, or long excerpts from, many of the most important journal articles, monographs and books published in the past dozen years by leading economists and experts. They

are grouped into four main parts: agriculture and economic development in historical perspective; measurement problems in the agricultural sector; theoretical aspects of agriculture in economic development; and aspects of the process of change in agriculture. The editors contribute an explanatory introduction to each part, outlining the evolution of economic thought on the main subjects discussed in the selections and indicating their importance both to students of and practitioners in the development process. A selected bibliography is included.

Ward, Barbara E., editor, Women in the New Asia; Paris, UNESCO, 1963, 529 pp., US$8.00.

The changing status and role of women in the developing countries have so far received very little specific attention in the literature on development, and this book is a major contribution toward filling this gap as far as the less developed countries in Asia are concerned. Conceived by UNESCO as one of the studies in its Major Project on the Mutual Appreciation of Eastern and Western Cultural Values, this study was organized and edited by Barbara Ward, who also wrote the long essay on "Men, Women and Change" which forms Part I of this volume. Part II consists of papers by Asian and Western social scientists on various aspects of the changes in the status of women and in male-female social relationships in individual countries of South and Southeast Asia. Also included are a number of autobiographical papers by outstanding Asian women. Part III contains background historical and demographical information, including appendices on the existing state of women's rights and on measures for family planning in the countries under study.

Abrams, Charles, Man's Struggle for Shelter in an Urbanizing World; Cambridge, Massachusetts, the M.I.T. Press, Massachusetts Institute of Technology, 1964, xi and 307 pp., US$7.95.

This is a comprehensive survey of contemporary problems of providing adequate housing in developing and developed countries. The author is an expert, long experienced in this field, who has travelled widely during the past decade and served on numerous survey and technical assistance missions in all parts of the world. His study covers the main aspects of the housing problem -- economic, social, governmental, administrative, financial and technical -- and examines not only difficulties but also the means which have proven effective in tackling them.

This study was sponsored by the Joint Center for Urban Studies of the Massachusetts Institute of Technology and Harvard University.

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